

RETAIL DISTRIBUTION REVIEW (RDR) INTERIM FEEDBACK REPORT

The FSA has published its interim report on the Retail Distribution Review (RDR) - the final feedback will be published in October 2008. The FSA is not looking for formal responses to this report, but welcomes comments

1. INTRODUCTION

The RDR is a central part of the FSA's overall strategy for the retail market, and is part of Treating Customers Fairly (TCF). The interim report sets out some new thinking:

- a clear distinction between advice and sales;
- higher professional standards (possibly overseen by a Professional Standards Board); and
- a new non-advice generic national service called "Money Guidance".

However, it also notes that it may not be possible to completely distinguish between advice and sales in practice, but wants to explore "how close" it can pragmatically and practically move towards this goal.

2. KEY POINTS

2.1 Changes to Original Proposals

Feedback has caused the FSA to simplify its ideas. The new "regulatory landscape" will consist of three strands – advice, sales and money guidance, as follows:

2.2.1 Advice

The major change is that the FSA is now planning only one type of professional adviser. However, there would be a step-change in the requirements for them. These would include:

- independence - operating remuneration without provider input (this means a move to factory-gate pricing);
- operating across the whole of the market. This has major implications for firms which are currently agents of providers (tied), and the sales forces of providers (such as bank, building society and insurance company staff) and multi-tied firms; and
- higher professional standards.

2.2.2 Sales

The FSA wants to separate sales into a service that is "strictly non advised". It would give more guidance to firms, to allow them to understand and operate guided sales systems and business propositions with very limited regulation.

2.2.3 Money Guidance

This is linked to the Pathfinder work that the FSA is currently working on, following the Thoresen Review. This service is intended to offer impartial information (only) and guidance on money matters – usually on simple issues such as credit card management, debt, simple savings etc. This would include opportunities for self service but it is not completely clear yet how this would operate.

3. AREAS OF DEVELOPMENT AND UNCERTAINTY

There are a number of areas of uncertainty that have not yet been resolved, although the FSA has given some indication of its thinking.

3.1 Clear and clean distinction between "sales" and "advice"

The paper discusses the potential consequences of making a clear distinction between sales (non advised) and advice. However, because there are many players in the market which have tied, direct or multi-tied business models, the FSA notes that it would need to take action to allow firms to develop sales services that include some element of advice – because of this it may not be possible to separate these services.

3.2 Provider Business Models

There is a clear statement that the FSA does NOT plan to ban commissions. However, it wants product providers to change their business models so that they do not determine how much advisers are paid. It is not clear how providers might achieve this or how the FSA might prevent moves to retain influence over outcomes. The question of whether the market can move back to a maximum commission system has been raised, and the FSA has noted that it is in discussion, over this and other matters, with the Office of Fair Trading.

3.3 Professional Standards

The original RDR proposals were that professional advisers would belong to a professional body. However, the FSA notes that it may not be able to make membership of a professional body compulsory because of the implications of competition law. However, it has challenged the industry to develop a market-led solution to developing a common set of professional standards – there are some indications that this may be delivered through an industry-wide initiative underway, and the FSA will facilitate discussions on this.

4. IMPLICATIONS FOR INDIVIDUALS AND FIRMS

4.1 Increase in adviser qualifications

The report proposes that individuals would have to achieve a higher level of basic qualifications – although the original proposed level has been reduced –and there will be greater emphasis on ethical standards. It is not just a matter of exams. A professional standards board may be formed.

The FSA does not believe that grandfathering (allowing currently practising individuals to continue in business by virtue of their experience rather than requiring them to obtain all the qualifications that a new entrant would require) should be a feature of these proposals, although they are willing to see this debated more fully. This will mean a significant investment by firms and individuals to achieve diploma qualifications across the board.

4.2 Changing Provider Business Models

The way in which providers, including fund managers, might change their business models, and the implications that this might have for financial advisers is not clear.

4.3 Impact on fund management style firms

The FSA has specifically stated that it sees investment firms of all types (including financial advisers, stockbrokers etc) as being affected by its plans. The implication is that firms offering investment services could become more distinct from firms distributing packaged savings and protection products only, which could cause some changes to the market infrastructure.

4.4 Impact on Mortgage Brokers and General Insurance Brokers

There are no current plans to extend the scope of the RDR to these firms. However, there will be a wider review of the Mortgage Conduct of Business (MCOB) regime and some changes might well be proposed at a later date.

4.5 The “Regulatory Dividend”

The FSA has noted that it plans to explore forms of incentives, including non-monetary regulatory dividends, for all types of firm to deliver good consumer outcomes. This is not likely to mean an automatic reduction in supervision for firms made up of advisers with high level qualifications alone. It is probable that examination of their systems and controls, as well as meeting higher than the minimum requirements on examinations, and other factors, will be necessary. This will include engagement with the TCF process and delivering outcomes that the FSA is seeking across a number of areas.

5. WHAT NEXT?

- The FSA will undertake research into the economic impact of some of its plans.
- A further, formal, feedback statement will be issued in around six months time (October 2008).
- Further detailed proposals will be put forward at some time after that. The FSA has noted the need for adequate transitional arrangements.
- The FSA is undertaking a thematic examination of intermediaries' use of platforms, to assess current market practice.
- The FSA is beginning a series of visits to firms to assess how they are meeting the TCF requirements. The findings of these investigations are likely to affect the FSA's thinking on what needs to happen on this issue as well.

6. FURTHER INFORMATION

The interim report can be found on the FSA website at the following link:

http://www.fsa.gov.uk/pubs/discussion/rdr_interim_report.pdf

The FSA has also issued a companion Feedback Statement (FS08/2) following the review of the capital requirements for personal investment firms contained in DP07/4, which is also relevant to firms. A separate article on this was included within the most recent Retail Compliance Bulletin. The feedback statement may be found on the FSA website at the following link:

http://www.fsa.gov.uk/pages/Library/Policy/DP/2008/fs08_02.shtml

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