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RETAIL DISTRIBUTION REVIEW: THE FINAL RULES

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Overview

The FSA's Policy Statement PS 10/6, published on 26 March 2010, sets out the final rules for implementing key elements of the Retail Distribution Review (RDR) intended to improve clarity for consumers about advice services and to address the potential for remuneration bias. The Policy Statement also sets out FSA's position on 'Simplified Advice' and non-advised distribution methods. The new rules and guidance will come into effect at the end of 2012.

Detail

The FSA are to go ahead with the vast majority of the proposals as drafted in the original Consultation Paper (CP 09/18) and there are few changes to the final rules from those that were proposed. The most important new rules will be those requiring firms to describe their advice services as either 'independent' or 'restricted' and those that implement the system of 'Adviser Charging'. From the end of 2012, adviser firms will no longer be able to receive commissions set by product providers in return for recommending their products, but will have to operate their own charging tariffs.

The range of products to which these rules apply has been widened when compared to current rules, to include all retail investment products as proposed, covering collective investment schemes, all investments in investment trusts and packaged products. This links into the European Commission's PRIPS (Packaged Retail Investment Products) review. All firms providing independent advice will be required to evidence that they have conducted a comprehensive and fair analysis of the wider range of retail investment products. Firms making use of panels can exclude certain products, but must demonstrate there is a valid reason to do so: the onus of proof will be on the adviser firm to show that there is not a product outside the panel that would meet the customer's demands and needs.

Firms will have to provide clear disclosure in a durable medium as to whether they are offering 'independent' or 'restricted' advice. A firm providing 'restricted advice' will in addition be required to provide oral disclosure to a client, but the FSA highlight that the proposed requirement for this to be via a mandated form of words is not to be implemented in the final rules. In practice, this translates to the proposed form of words appearing as guidance rather than rules in the made handbook text.

Advisers will have to set their own charging structures, and these should not vary for inappropriate reasons. The tariff must be provided to the customer at the outset, along with the total adviser charge. The FSA are in discussions with trade bodies and firms to determine if there is a need to publish examples of good and poor practice in developing appropriate charging tariffs over the next few months.

Since the ‘Adviser Charging’ rules will apply to business conducted after the end of 2012, there will be practical implications for firms in distinguishing legacy and new business, in order to determine from where legacy commission can still be received. This issue is further complicated where there is a change of adviser.

Industry feedback

The industry feedback set out in the Policy Statement includes concerns that the banning of ‘factoring’ (where a product provider pays the adviser the full amount of their adviser charge upfront at a discounted rate and then recovers this payment over time through the product) would reduce customer access to low-cost regular savings products. The FSA have stated that advisers have the option of allowing customers to pay for initial advice over time for regular contribution products and therefore have gone ahead with the ban on factoring. The fundamental point is that the cost of the advice must be agreed between the customer and the adviser, not between the adviser and the product provider.

The feedback also highlighted significant concerns with the proposed rules on ‘Basic Advice’, ‘Simplified Advice’ and non-advised services. It was felt by some that the changes could reduce consumer access to advice, with fewer people willing to pay. There will not be a new regulatory regime for Simplified Advice, as agreement across the industry has not yet been reached. The FSA remain engaged with the industry on whether a lower qualification standard would be appropriate for Simplified Advice, mindful of the feedback from IFAs that this may give bancassurers an unfair advantage.

There were also concerns expressed that firms may label sales incorrectly as ‘non-advised’ in order to avoid the new Adviser Charging rules. The FSA have stressed that they will be checking via supervision that the rules are not being circumvented and will be conducting a post-implementation review to assess the RDR’s success in achieving the desired outcomes after 2012. To avoid the rules being circumvented by separating advice from related services, new guidance has been added to the final handbook text explaining that arranging or executing a transaction and conducting administrative tasks are also subject to the adviser charging rules. This is likely to present some practical difficulties in interpretation.

Throughout the Policy Statement there is mention of negative feedback to certain of the proposals, in particular from distributors operating a business model which differs from that of a “normal” IFA, and from investment management firms that suggest practical difficulties in implementing the new rules. There are also numerous references to a ‘majority of respondents agreeing with proposals’. So the firms that will face the biggest challenges it seems will be those that are smaller, niche or bespoke, and possibly in the minority. For firms that do not decide to exit the industry, the publication of final rules at least means that planning the required changes to business can be undertaken with certainty.

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