

Financial Services Authority

Consultation Response

Retail Distribution Review - DP10/02



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1 EXECUTIVE SUMMARY

As a discussion paper DP10/2 is clearly looking to encourage feedback and it has certainly succeeded. There are some bold positions outlined in the paper, which have ignited debate and attracted considerable comment from across the industry.

Whilst most of the key arguments in the paper have been well constructed, there is a sense that they are not quite joined up and some interesting issues emerge when they are considered in combination.

The most striking example is the interaction between the proposal to ban payments from providers to platforms and the mandating of platform re-registration. The fallout from the first of these will be multiple share classes which unintentionally pulls the rug from under the second.

In our response to the discussion paper we have attempted to take a step back to look at these interactions between the different proposals and the operational consequences that flow from them.

2 INTRODUCTION

As an enterprise architecture consultancy specialising solely in Financial Services, Altus has extensive experience working with clients in the LP&I sector including platform operators. With practical involvement in both system and business issues throughout the sales process we welcome this opportunity to respond to the FSA's latest discussion paper on the Retail Distribution Review.

Our focus is primarily on the operational aspects of financial services and we have sought in the following sub-sections to answer those questions raised in DP10/2 where we feel our experience and expertise particularly qualifies us to do so.

3 RESPONSE TO PARTICULAR QUESTIONS

Q1: Do you agree with our analysis of the issues related to platform remuneration?

The summary of different platform remuneration models is admirably clear and concise. There is however, one issue in the analysis that we would like to comment on concerning the question of what rebate payments are for.

The conclusion reached in the discussion paper is that rebate payments from providers to platforms are to secure distribution rather than for utility services. Evidence for this view is offered by the statement in 3.20 that “administration services the platforms usually provide are a by-product of platforms effectively converting multiple direct investments into a single nominee investment.”

Whilst this is true, there is no reason why a platform has to be built this way to offer consumers the ability to manage their investments in one place. Platforms are built this way, at significant cost, precisely because the aggregation of multiple small investments into a single high value deal allows the platform operator to negotiate better terms with the provider (who benefits from the reduced administration of fewer but bigger investments). A platform could simply pass individual deals to the provider and operate as a conduit to the consumer, relieving themselves of the overhead of effectively managing a sub-register of investors.

To be clear; we do not agree with the analysis that current platform services are an inevitable by-product of being a platform. Platforms do perform complex activities on behalf of a provider but that’s because there is a revenue stream associated with doing things that way and not because it is the only way they can operate.

Q2: Do you agree with our preference to stop payments from product providers to platforms? If not, please explain why and how any alternative proposals would be consistent with the objectives of the RDR.

We agree with the RDR principle of separating product and advice costs and we appreciate that the preference to stop payments from product providers to platforms is an attempt to apply this principle. Unfortunately, in our opinion, this proposal would lead to a significant increase in complexity (and cost) for both fund administrators and platform operators due to the proliferation of share classes we believe would result.

As a minimum, fund managers would need to add one new share class per fund to accommodate post-RDR units alongside current holdings (this may be required anyway for non-platform business). In practice we believe there would be many more share classes as platforms seek to negotiate individual deals which recognise their scale.

This proliferation would increase complexity for advisers who would need to trade-off the different costs of units in the same underlying fund against the various platform charges involved in accessing those units.

More importantly it would increase complexity for consumers who will be faced with the prospect of holding units of different value (at least pre- and post-RDR) in the same fund. Presenting such information clearly for consumers will be quite a challenge.

A further unintended victim would be the case for re-registration made so strongly elsewhere in DP10/2. Re-registration is based on the concept of in-specie transfer of the same asset to a different nominee. By effectively ensuring that any assets held on platform after 2012 will be of a different share class to those held currently this proposal ensures that any transfer after 2012 of pre-RDR platform assets to another platform will involve selling and buying units – precisely the outcome DP10/2 sought to avoid by mandating re-registration.

The situation would be unlikely to improve much after 2012 if different platforms end up, as we suspect, with their own unique set of share classes.

Q3: Should any changes to platform remuneration also apply to non-advised business? Please explain your answer.

At a practical level, this issue will manifest itself where the same platform is used to support advised and non-advised business for the same customer. To date this has seemed an unlikely scenario but has become much more realistic with the advent of corporate wrap platforms.

Whilst the early focus of most corporate wraps is group pensions (which are covered by RDR), several are also looking to include the other most common investment vehicle, ISAs on a non-advised basis. If non-advised business were to remain outside the scope of RDR, an employee using a corporate wrap may find they have units in the same fund via two different tax wrappers performing in significantly different and potentially confusing ways.

Q4: Do you agree with our analysis of what will be required to facilitate Adviser Charging through platforms?

The analysis is sound but the practical consequences will be daunting for platform operators. Standards will need to be established for communicating adviser charge instructions and validating those instructions will require a secure channel with the customer, which many retail platforms aimed at advisers will not have established.

Where initial advice fees are paid in installments via adviser charging, platform operators will need to be very clear over their obligations in respect of any unpaid charges. This will be particularly important if the consumer opts to exercise their rights to stop the payment of ongoing fees as described in 3.37.

The requirement to consider potential tax consequences of charge deductions could also be very onerous depending on how it is applied. If the requirement is simply to disclose the potential effect of a standard approach then this could be easily accommodated. If the platform operator were required to vary their approach on a case by case basis then this would be much more complex.

Q5: Do you have any comments on the application to platforms of our intention to end product charge rebating?

This point would be redundant if payments from product providers to platforms were stopped as suggested in 3.25. However, for reasons discussed above, we do not believe that option is viable.

In our view product provider payments to platforms should be permitted, they should be transparent and fully rebated to the customer's cash account with advice and platform fees separately charged. Ideally there would be one retail share class (stripped of advice costs) for each fund making comparison of platform costs a relatively simple exercise. We believe this represents the most practicable way for consumers to benefit from a platform's buying power and to make informed decisions on the trade-off between platform charges and access to cheaper funds.

That does not mean we think current approaches to rebates are perfect and we would expect the FSA to regulate in this area to ensure consistency of approach across providers and platform operators and to ensure clear disclosure to the consumer.

Q6: Do you agree with our analysis of the issues relating to inducements and our approach to inducements provided by platforms? If not, please explain why not.

The analysis in the discussion paper is clear and sensible but the reference to COBS 2.3 may give rise to some confusion. COBS 2.3 is aimed at the direct relationship between product providers and adviser firms and the reasonable non-monetary benefits table is written from that perspective. The table does not include the type of analysis and planning tools which are an integral element of most platforms and which deliver a key part of the service they provide.

The status of platforms is discussed in 3.6, which acknowledges that a platform is a service not a product and perhaps it would be useful to revisit the inducements rule in light of this.

Q8: Do you agree with our approach to the issue of re-registration?

Altus strongly supports the idea of automated solutions for re-registration, which we believe would benefit both platforms and consumers. Unfortunately, the potential demand for such solutions could be unintentionally undermined by other proposals in the discussion paper – see our earlier answer to Q2.

Q10: What is your view of the services currently offered by platform operators to provide investors with information about their investments? Do investors receive enough information and do they receive it in good time?

In our view the services currently offered by platform operators are limited but appropriate for the vast majority of investors who are not interested in receiving additional information and would be unlikely to exercise their voting rights.

Q11: Do you agree that where platforms do not host funds with non-standard features or tax regimes, this could lead to poor outcomes for consumers? Please give reasons for your answer.

This would only be the case if advisers were limited to advising on platform assets. As the discussion paper explains in 3.63, independent advisers must consider off platform investments as well.

Q12: To what extent should platforms be required to give product providers information about the end investors?

In our opinion any such obligation should be limited to what is practical and easily achievable. Since platforms already maintain a sub-register of investors, it should be relatively simple to provide investor numbers and average/maximum holding information.

Any requirement to provide greater detail than this could have the side-effect of making re-registration more complex and might undermine the work currently being done on developing message standards for this area.

4 ABOUT ALTUS

Altus is a business and systems solutions company focused exclusively on the needs of the financial services industry. Our practical experience of both the business of financial services and the supporting IT systems means that we can help solve the right problems with the right technology. Our mission is to be at the forefront of the networked financial services business of the future.

Our management team has extensive experience across a wide range of financial services activities, our staff are highly-skilled and enthusiastic and our client list includes some of the largest financial services companies in the UK and Europe.

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