



The Actuarial Profession

making financial sense of the future

consultation response

Financial Services Authority's *Review of Retail Distribution*

**Response from the Financial Consumer Support Committee
of The Actuarial Profession**

December 2007

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A Committee of the Actuarial Profession**

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The Financial Consumer Support Committee (FCSC) considers matters of interest to the Actuarial Profession which have a particular bearing on consumers. The Retail Distribution Review has the potential to deliver significant benefits to many consumers as well as to the financial services industry. Many other organisations will focus on the implications for the industry. This short response focuses specifically on the potential impact on consumers.

Key points

- The FSA is right to be considering alternative distribution models which can better meet the needs of a wider sector of the population
- Any new approaches need to be considered alongside the introduction of Generic Financial Advice
- Primary advice, as currently described, continues to look across a range of possible customer needs, whereas many consumers want financial guidance relating to a specific life event
- We believe the best way to address the current gap in the market is to develop and improve the concept of focused advice to fill a current gap in the market
- Alongside this, it is important to clarify the responsibilities of consumers, as well as advisers and providers

The background to the issues

The FCSC welcomes the Retail Distribution Review and agrees with much of the rationale which has prompted it. We agree that the current model does not serve all consumers well and particularly welcome the elements of the review which consider how to address this by introducing new distribution models.

We believe the review should start with an analysis of what consumers need against what is currently available to them. In view of the likely timescales for implementation, it is important to factor in other initiatives which are in development. The most pertinent development is the Generic Financial Advice service being developed by the Thoresen Review. We can then concentrate on how best to meet any remaining gaps. Our overall impression of the review is that some of the proposals have an undue focus on the 'internal industry issues' surrounding the delivery of advice, often losing sight of what consumers actually need.

It is widely acknowledged that there is a major gap in consumers accessing 'advice and guidance'. This is both a demand side issue (consumers often do not wish to face up to their financial futures) and a supply side problem (it is accepted that regulation has driven up the cost of providing regulated advice making it unfeasible to serve consumers with relatively small amounts to invest). We strongly support the Generic Financial Advice concept as a non-regulated support service. But however successful its implementation, it cannot – nor does it set out to – fill all of the gaps.

As explained in the Thoresen Review's interim report, the service will be available to all, but will focus on the 19.2m that would benefit most. It will not represent regulated advice and it will not recommend any particular product or provider. Instead, it will equip individuals to make better informed decisions and point them to what to do next. This is likely, in many circumstances, to involve seeking regulated advice of one form or another. So it is vitally important that the Retail Distribution Review considers how the current advice market can be improved and extended to dovetail with Generic Financial Advice.

What do consumers actually want?

It is important to base any new advice models on what consumers want or need in terms of financial 'advice'. Here, we deliberately avoid using the narrow definition of regulated advice and instead consider what consumers would more generally understand by 'advice'.

Research carried out by the Resolution Foundation identified four specific need types, which it categorised as follows:

1. People who want to purchase a financial services product and need to access a 'trusted sense maker'. In particular, people do not know which product to consider, how to compare product pricing, how to source products, and need help in understanding product information and application forms.
2. People who get married, start a family, retire or experience some other major transition in their lives often need assistance to help them deal with the financial implications.
3. People who find it hard to meet their normal expenditure, especially debt repayments, often need guidance to assist them at a difficult time.
4. People who need better financial management and to review their income and expenditure and the interest rates on their borrowings and savings. They may not know how to do this or may lack access to the tools and information they need.

What is most striking from these findings is that a consumer's need for guidance or advice is frequently event driven. This is in contrast to the current regulated advice model which centres around 'know your customer' requirements and as a result looks across all areas of financial need. This model serves many consumers very well, and consumer surveys often demonstrate that holistic financial and tax planning is desirable. However, this is a counsel of perfection which is unlikely to be available or affordable across all earnings or wealth bands – and in many instances, is simply not necessary. It is this gap we need to target new models on.

In practice many consumers are looking for advice relating to a specific need, generally relating to a life event (house purchase, starting a family, retirement or divorce). There is a strong and understandable tendency for consumers to want to focus on their immediate needs, without being distracted into considering their wider or longer term needs. In other words, when a consumer is buying a house, the mortgage is the primary concern because it is the means of buying the house. In practice, a financial adviser who tries to broaden the discussion can find it difficult to engage the customer even in a related subject such as term assurance, and often impossible to engage the customer in a wider discussion about savings and pensions.

Primary Advice

The principal suggestion in the Discussion Paper for a new distribution model is Primary Advice. This appears to be a 'cut price' version of full financial advice which would continue to consider a range of simple products designed to meet simple needs. The Review acknowledges that "products bought as a result of that advice are not necessarily the most suitable but are better than if the product hadn't been bought at all." In our view, this is not where the main gap in the market lies. We believe a model that focuses on a particular need would be better aligned with what consumers want.

While we appreciate we are currently only at discussion phase, we have concerns that Primary Advice may cause confusion with consumers. At present, customers can have difficulty understanding the difference between information, guidance and regulated advice. Great care will be needed if we are to have two forms of regulated advice in future. It might make sense to research with consumers how best to assign meaningful labels to different services. We note the Thoresen Review has indicated its service will not ultimately be called Generic Financial Advice. We welcome this, particularly to avoid confusion with other forms of 'advice'.

Focused advice

We believe, therefore, that rather than considering a new regulated regime that provides a cut down version of full financial planning, the focus should be on delivering what the majority of consumers currently excluded from the advice market actually want and need - cost effective guidance relating to a specific life event.

We understand the temptation to propose financial planning in preference to more focused advice. There is a sound argument that there may be different product solutions suitable for each life event, and advice should have regard to the wider needs of a customer (and any existing products that are held), but there has to be a trade-off between the ideal and the practical.

In the vast majority of circumstances, the benefits of providing an immediate solution to what the consumer thinks he or she wants will outweigh any potential downside from not having considered all other needs. Moreover, consumer detriment is likely to be greater if the outcome is to provide nothing at all rather than what a consumer wants.

Mis-selling incidents of the past have led to our industry being very cautious about risk-taking. This is understandable, but the balance may have swung too far, leaving us in a position where our industry is not delivering to what consumers actually want. The FSA's move to more principles-based regulation provides an opportunity to move away from cautious following of prescriptive rules, but will only deliver more flexible consumer services if there is a willingness by both FSA and industry to experiment.

In our view, FSA regulation already includes the core concept we need to better deliver to customer wishes in the form of focused advice. This form of advice sits within the regulated framework, but allows advisers to concentrate on a restricted range of needs – provided this is made clear to the customer. However, many advisers lack confidence in using this approach and those who do err on the side of caution, which makes it not significantly less expensive than full regulated service. This restricts its availability and leaves many consumers excluded. We believe the solution lies in greater regulatory clarity and a willingness to focus more narrowly than at present. This, in our view, would offer a better solution to consumer wants than primary advice, particularly when we allow for the development of Generic Financial Advice.

We believe forms of focused advice could be delivered both

- outside current FSA regulation as a form of Generic Financial Advice where no specific product or provider recommendations are made and
- within FSA regulation with a product and provider recommendation being made, but with greater focus so it can be delivered more cost-effectively, making it accessible to a wider group of consumers

Consumer responsibilities

Our suggestions above concentrate on the 'supply side' of this new form of advice. As noted earlier, the advice gap is only partly a function of supply side issues. It also exists because of the lack of consumer engagement with or demand for financial services products and associated advice. It is essential that we continue to pursue financial education and capability initiatives to help stimulate consumer engagement and demand. We welcome the FSA's stated intention to explore consumer responsibilities in financial services transactions and agree that consumers should take some responsibility for their own actions. Whilst we do not advocate "caveat emptor" in its literal sense, it is equally unreasonable that consumers are able to avoid any responsibility for their financial decisions. The key issue is defining respective roles and responsibilities for consumer, adviser and provider. Treating Customers Fairly creates a framework for taking this forward. It also provides a powerful protection against the reintroduction of what are now seen as poor selling practices or unfair charges of the past.

Conclusion

In conclusion, we believe it should be possible to define new forms of 'advice' where the needs of the consumer are met more cost-effectively and access is increased. This should be accompanied by clear responsibilities of consumers, advisers and providers. Any 'lighter touch' regulatory regime can open up the prospect of the advice to some individuals being less optimal than under current full advice models. But we believe this can be more than compensated for by wider access, the greater availability of advice of a form consumers recognize they will benefit from, and hence many more people making sensible financial decisions.

We would be very happy to discuss any aspect of our response with you if this would be helpful.

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