

**Treasury Select Committee inquiry into The Retail Distribution Review  
Memorandum by the Investment Management Association**

**Executive Summary**

1. The Investment Management Association (IMA) represents the investment management industry in the UK. Its members manage £3.4 trillion of assets on behalf of a wide range of clients including pension funds, life insurance companies and investors in retail funds. At the end of November 2010 funds under management in UK-authorized retail funds stood at £555 billion. Almost 90% of retail fund investors now buy their funds through intermediaries, many of whom are impacted by the Retail Distribution Review.
2. We welcome the opportunity to contribute to the Committee's inquiry into the Retail Distribution Review (RDR) and would be pleased to supplement this note with oral evidence should that be of interest to the Committee.
3. The IMA has always supported the RDR's objectives of achieving greater transparency in the retail market in the interests of ensuring a better deal for consumers. Increased professionalism and enforcing professional standards will be critical to achieving the FSA's stated outcomes. We also support the objectives of the new rules on adviser charging: commission bias in the advice market has been a problem for many years and needs to be tackled. We fear, however, that the detailed proposals on adviser charging will not succeed in achieving the objectives of greater transparency and better outcomes for consumers. Their impact will vary between different participants in the market, and there is a real risk that this will distort competition by not providing a level playing field between different types of product and different types of firm. The ultimate result of shifting the balance of competitive advantage in this way is difficult to predict at this stage. But there is no guarantee that it will work to the benefit of consumers. We think there is a real risk that the outcome could be increased costs and less transparency for consumers.

**A transparent and fairer charging system**

4. We agree that the correct starting point for the RDR is to seek to remove commission bias from the decision-making process for giving financial advice to consumers. The principal change that the FSA is proposing is that adviser charging will have to be agreed with the consumer in future. But crucially a rule is also being proposed which would allow product providers to "facilitate" adviser charging out of the product. This raises the immediate prospect that advisers will demand that product providers continue to "facilitate" payments; as a result product providers will search for ways to allow them to continue payments to advisers and there is already evidence in the marketplace that certain firms are actively promoting to advisers mechanisms which will allow them to do so. This is tantamount to allowing commission payments to continue in another guise.

5. The impact of these rules will differ for different providers. In relation to investment funds, the current practice of paying trail commission will be prohibited, as the payments would not be being determined by client agreement. And funds cannot offer variable payments according to whatever terms are agreed between advisers and their clients because management charges are taken through a single daily price for the fund. Similar constraints do not apply however to many other investment products, which will be able to continue to offer payments in order to facilitate agreed charges due to advisers. Indeed we are aware of providers who are already making available to advisers their proposals for this once the RDR is in place.
6. Although this continuation of commission by another name is less than satisfactory, fund management firms had believed that they would be able to participate by means of payment to client cash accounts maintained by platforms, whose disbursement – whether to advisers or to the client's own portfolio – would be the subject of a separate agreement. But the FSA is also proposing a prohibition on rebates to clients. At the same time, however, there will be no corresponding prohibition on rebates to other intermediaries such as platforms, life companies and execution-only services. Life companies will hence be enabled to have access to cash with which to pay advisers.
7. This will significantly shift the balance of competitive advantage in the distribution of investment products. It will, for example, create an unlevel playing field between “unwrapped” funds and other products like funds which are sold via intermediaries such as fund or life insurance platforms, because the latter will be able to make use of rebates to facilitate adviser charging. Such payments will be less transparent than a disclosed annual charge. Suggestions have been made in the industry that the lack of ability to offer client rebates may require funds to consider allocating extra units which could then be redeemed for the purposes of paying advisers. Again, this would be complex to administer and lead to additional costs and opacity for the consumer. An alternative would be for wrapper providers to levy a separate charge for the wrapper in addition to the underlying investment charge; not only does this risk being opaque but it will also lead to extra costs for the consumer. The net effect will be a shift in competitive advantage between funds and life insurance savings; between wrap platforms and fund supermarkets; and between advisers who will not be allowed to receive rebates for ongoing services and non-advised intermediaries such as execution-only brokers and banks' sales teams (as opposed to advisers) which are outside the scope of the proposals.
8. In addition, from a tax point of view consumers will have to pay VAT on fees to their advisers, paid from investment income which has already taxed rather than paying for it out of their investment contribution and not having to pay VAT.
9. Overall, there are real risks that the outcomes sought by the FSA will now not be achieved and that instead the result will be higher charges for consumers, continued high initial payments to advisers, increased complexity and opacity for consumers and an uncompetitive marketplace.

### **A better qualification framework for advisers**

10. It is clear that a better qualification framework for advisers will contribute to improved standards of professional advice. We therefore support the FSA's proposals that all advisers should meet a basic minimum standard. It is also right that advisers should

maintain higher standards through CPD which is both relevant to their needs and effectively monitored. However, raising the bar in terms of entry level examinations and CPD will not of itself deliver significant improvement in consumers' trust and confidence in financial services. To ensure that the RDR changes are effective, they should be communicated to consumers through a planned campaign which includes evidence of the value of advice and guidelines on how to recognise good quality advice. The FSA, together with industry practitioners and associations, should positively promote the changes and what they will mean to consumers.

### **Greater clarity about the type of advice being offered**

11. We agree that consumers should be made aware of the distinction between independent and non-independent advice in line with the proposed new disclosure requirements.
12. It is also important that advisers should clearly disclose the basis of their non-independence, i.e. whether it is through their employment by a larger organisation (for example some retail banks offer only a small number of providers' products) or because they have chosen to restrict themselves to a set part of the market. In the latter case, it should be made clear that this is their choice and does not represent an endorsement from the product providers whose products they have chosen to offer.
13. The FSA should also take account of non face-to-face advice, such as online advice, for which a requirement to disclose the type of advice orally would not be practical.

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