

17 February 2011

Anita Flannigan  
Conduct Policy Division  
Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
LONDON E14 5HS

Dear Anita

**CP 10/29 Platforms: Delivering the RDR and other issues for platforms and nominee-related services.**

IMA represents the asset management industry operating in the UK. Our Members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of over £3.4 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles. In particular, our Members represent 99% of funds under management in UK-authorised investment funds (i.e. unit trusts and open-ended investment companies).

It is as providers of authorised retail funds that our members are interested in the role of platforms in the distribution chain and have comments on the proposals contained in this Consultation Paper relating to platforms and other intermediaries, and on the proposed ban on rebates of annual management charge (AMC) to retail investors.

IMA has from the outset supported the RDR's objectives of achieving greater transparency in the retail market and a better deal for consumers. However, it is our view that the way in which the RDR proposals on adviser charging have developed, and the impact of the draft rules in this CP in particular, will lead to a distortion of the market. They do not provide for a level playing field between different types of product and between different types of distributors. We remain concerned that the balance of competitive advantage will be shifted in such a way that will not benefit consumers. In fact, we are firmly of the view that the FSA's latest proposals in this CP will have the perverse effect of leading to increased costs and less transparency for consumers. We expand, again, on these points in the attached.

We continue to believe that those rules already finalised, which place new and specific obligations on advisers and product providers as regards qualifications and the provision of clear, fair and misleading information for consumers on charges, will have a major impact on the retail market place and will achieve in large measure the objectives of the RDR. It is, in the main, the more recent proposals that cause us concern. **We therefore urge the FSA to reconsider the proposed ban on rebates of AMC and, instead, to review the necessity for such a ban once the impact of the other new rules is known.**

Also, there remain a number of areas where clarification is needed (see below) before fund managers can sensibly take firm, business-critical decisions about new share classes and other matters. Not only is this causing delay to our members' and intermediaries' implementation plans, it will result in a raft of work in a short time period for the FSA's fund authorisation team in processing the various pieces of new fund documentation that will be required.

Our detailed response to each of the questions contained in the CP is attached. In addition to our concerns about the effect of the ban on rebates of AMC to consumers, we would highlight three other points:

#### Execution-only business

It is hard to understand why the FSA has decided that it will continue to permit the payment of commission for non-advised business, particularly given its stated belief that it is desirable for there to be common standards for advised and non-advised business. This outcome will require the maintenance of extra, commission-paying, share classes by fund managers and, since no record is held of whether a sale is advised or execution-only, payments from these share classes will have to be validated on each occasion. There is also the danger that business may be placed under the guise of execution-only so as to generate a commission payment.

#### Legacy book

The difference in treatment of the legacy book and new business will create considerable complexity and, arguably, considerable consumer detriment for current fund holders. Under current proposals the fund management industry will continue to pay trail commission *ad infinitum* on legacy business and maintain a different book for new (post-RDR) business. Yet it still remains unclear what constitutes new business and what sort of activity would necessitate a move to the new regime. We note some of the scenarios in the attached.

Equally, the current proposals may result in some consumers' fund holdings not being reviewed, leaving them in unsuitable investments purely because they continue to pay trail commission. Conversely, those many advisers who act in a professional manner will have to attempt to explain to their customers the hideous complexity of a portfolio that is part legacy business and part post-RDR business, including as regards their payment being part VAT-able and part VAT-exempt.

We believe it important that the FSA reassesses its position regarding risks to consumers arising from its policy concerning the legacy book and we urge the FSA to provide clarity on how different legacy investments should be treated.

#### Drafting issues

In addition to these policy concerns, there is a number of places where the draft rules will not actually deliver what the FSA has said it intends. These are detailed in the attached and include key rules such as:

- the rule on obtaining and validating instructions from the retail client, which, though amended, still fails to recognise that with intermediated business the fund manager does not have any direct communication mechanism with the investor;
- the exemption for regular contribution products which continues to work only for insurance contracts;

- the definition of intermediate unitholder, which fails to capture properly the intermediation chain; and
- the use of the phrase “acting as a nominee company”, which does not fit with the definition of a nominee in the Handbook Glossary.

We would be grateful for an early meeting with the FSA to discuss the points raised in our response.

Yours sincerely

A handwritten signature in black ink, appearing to read "Andy Maysey". The signature is stylized with a large, sweeping underline that loops back under the first name.

Andy Maysey  
Senior Adviser – Retail Distribution

## CP 10/29 – IMA's responses to the FSA's questions

### **Q1: Do you have any comments to make with regard to our definition of a platform service and platform service provider (contained in Appendix 1)?**

The platform proposition has, in the past, been used to describe a range of business activities which includes those undertaken by fund supermarkets and wrap providers. We agree therefore that it is important that a coverall description be devised to capture those links in the distribution chain that are intended to be captured by the proposed rules in this Consultation Paper.

### **Q2: Do you agree with our proposal to read across our rules on product providers to platforms in relation to facilitation of payment of adviser charges?**

The change to 6.1B.9 R – specifically, the addition of the words “or otherwise by means of a *platform service*” – is helpful but does not address the issue on which we have previously commented to the FSA. Where there is a platform or other intermediary involved which holds units in a nominee account, the manager cannot obtain and validate instructions from the retail client as they have no knowledge of who they are. We had understood from previous discussions that this rule would be amended to allow the manager in these circumstances to rely on the platform or other intermediary that is facilitating adviser charging as having the obligation to obtain and validate the client's instruction. We ask again that this rule be amended.

Clearly, where managers are dealing direct with investors, they will have the obligation to obtain and validate the client's instruction where they are offering to facilitate adviser charging. We would note that, an increasing proportion of this business (as well as that conducted via platforms) is conducted electronically. We read the rules as allowing for validation via a range of media. We seek the FSA's confirmation that this is the case.

We also support the proposal to extend the rules so that platforms facilitate the collection of adviser charging to the same standard as that expected of providers.

In the CP the FSA continues to make reference to the establishment of a platform cash account as a straightforward way of platforms facilitating adviser charges for the consumer. However, the proposed prohibition on rebates of AMC to retail consumers effectively means that the funds industry will not be able to facilitate adviser charging in a way which is clear and transparent to consumers. Fund investors will therefore have limited mechanisms available to them to ensure that the cash account has sufficient funds to meet the ongoing adviser charge (see answer to Q.6 below).

### **Q3: Do you agree with the rules and guidance we have proposed in relation to the standards we expect from an adviser when using a platform and providing advice?**

**Q4: Do you have any comments on the proposed guidance, on the use of platforms and the independence rule, in Annex 5?**

It is important that advisers offering a whole of market proposition should be able to offer the facilities of an appropriate platform service for each consumer in line with their needs. Platform services generally have access to a wide range of funds, but not whole of market. For example, retail (as opposed to wealth management) platforms commonly do not offer tax-efficient funds for use in ISAs and personal pensions, or ETFs or investment trusts, and have the option under existing regulation never to do so. Also, the choice of personal pensions and SIPP on platforms is limited. All these factors, and others, will make it difficult, if not impossible, in practice for advisers to meet their whole-of-market obligations for any client by using one platform.

We generally agree with the guidance offered in Annex 5 to the CP, particularly with respect to considering products off-platform etc, and suggest that this should be the benchmark for advisers where using platforms.

However, the whole of market is extremely wide, and solutions to a consumer's investment situation could be quite diverse. Therefore the FSA needs to be pragmatic in its approach to appropriateness and suitability. It may well be that a number of investments offer broadly similar outcomes - each of which are suitable.

More to the point, platforms should be encouraged to offer the widest choice of products to market and, indeed, be discouraged from adopting practices that might limit such a choice, through size or cost etc. This would ensure the widest availability of products to advisers and, in turn, offer a better service to consumers. Unless these issues are dealt with, one of the central objectives of the RDR (to ensure a level playing field) will not be achieved.

In our response to DP 10/2 we drew the FSA's attention to some areas of potential consumer detriment arising from adviser activity associated with platforms. We repeat these concerns below as we see little in the CP which addresses them.

Regular premiums/payments

We have commented previously that, as drafted, rule 6.1A.22 (2) enables advisers to recover adviser charges through the sale of regular premium (i.e. life) products only, due to the explicit reference to contracted payments. We understand that this is not the intention behind the rule and ask the FSA to amend it so that it covers also regular contribution savings schemes in other sectors, including, as follows

"6.1A.22 R (2) the *adviser charge* relates to a *retail investment product* to which the *retail client* has ~~contracted~~ **agreed** to contribute ~~to~~ regularly over a period of time....."

Such a change would enable an adviser charge to be payable over time through such investment vehicles as ISAs and regular savings plans etc. If the rule is left unamended, it is likely to result in advisers favouring regular premium products simply so that they can achieve an income stream. This will also introduce unnecessary life cover into meeting savings needs.

## Legacy book

We would again urge the FSA to re-assess the risks to consumers arising from its current policy regarding legacy business. The FSA has indicated that advisers can continue to receive trail commission from business sold before the RDR rules on adviser charging take effect. Apart from the business strain this will impose on fund managers and third parties, who will need to maintain a back book of business *ad infinitum*, advisers will lack external motivation to review consumers' portfolios, as any change in portfolios will result in the cessation of trail commission and, with it, a steady income stream.

It is important that there is general agreement across the industry and with the FSA on exactly which transactions should be treated as legacy and which as new business. Fund managers, administrators and platforms will require clarity in a number of areas so that the correct action is taken.

For example, it seems that a fund switch on an ISA would be treated as new business and would no longer be eligible for commission. Conversely, we understand that a fund switch in an investment bond would not be considered to be new business and commission would continue to be paid. Indeed, we have become aware of this feature of an investment bond being promoted to advisers as a key element.

A similar disparity of treatment between the sectors will arise if the FSA persists with the view it has expressed to us on occasion that the ISA for a new tax year is new business. An ISA is no more than a tax allowance and reporting device. It is not itself a retail investment product. The holding in the fund held within the ISA is the investment. If the investment remains the same from one year to the next, why should that be regarded as new business?

If the trigger for determining the correct treatment is whether or not the consumer has been advised on the transaction, the fund manager/platform will not necessarily know this. If they have to ascertain this, the transaction could be delayed. There is also a danger that advisers will simply instruct their clients to give the instructions direct so that commissions can continue to be paid.

**Q5: Do you agree with our proposals for platform remuneration? If not please explain why setting out the effects of our proposal and what should be done instead, and why.**

A number of our members agree that platforms, like any other form of order aggregator in any market, should be able to benefit from bulk discounts. They therefore welcome the FSA proposal that rebates of AMC to platforms will not be prohibited. Others of our members, however, do not agree that platforms should be allowed to receive payments from product providers.

If payments to platforms are to be allowed to continue, it is essential that users of the platform – both advisers and their clients (the consumers) – should have clear information about what the platform is receiving, what impact that has on the price the consumers pay, and continue to pay, for the product, and in what other ways the platform is being remunerated.

We note, though, that the language used by the FSA in the box on page 10 of the CP is most unhelpful, especially in the context of discussions on the VAT treatment of payments going forward. Platforms do not provide administration services to fund managers, just as supermarkets do not provide administrative services to food producers. As we have repeatedly said, fund managers benefit from reduced administration costs as a result of the aggregation of order flow by platforms, as that aggregation results in a smaller unitholder register for the AFM to maintain.

**Q6: Do you agree with our proposal to ban the rebating of product charges in cash to retail clients across all retail investment products when advice is being provided?**

We continue to support the FSA's stated aim that one of the outcomes of the RDR is to remove commission bias from the decision-making process in the giving of financial advice to consumers. However, we do not believe that the current proposal to ban cash rebates to consumers will achieve the objectives of greater transparency and better outcomes for consumers. Indeed, we are of the view that it may lead to increased costs and consumer detriment through product bias.

In previous submissions to the FSA we have explained that fund managers use the AMC as a means of meeting the costs of both managing and distributing funds. Indeed, this is the only tool that managers have to do this given that their balance sheets and the funds are quite separate. To date, the sector has seen, and the FSA produced, no evidence of consumer detriment arising through this mechanism.

The impact of the removal of cash rebates will differ for different providers but will centre around the ability for any provider to facilitate adviser charging, as envisaged by Rule 6.1B.9. In the case of investment funds and platforms, the only mechanism open to them will be the redemption of units. As we have previously stated, the potential detriment arising from such a mechanism will include:

- The consumer being forced to redeem against the spread; and
- The difficulty in deciding from which funds to redeem units and at what frequency.

There will also be tax implications:

- Potential Capital Gains Tax liability – although not likely to be material
- In redeeming units to pay for an “ongoing service” from the adviser the consumer will incur a VAT liability on that service which is, currently, 20%. Therefore the units redeemed will need to amount to 120% of the amount to be paid to the adviser.

There is also the considerable administrative inefficiency of several small redemptions being used with the associated need for regular documentation to inform the customer, simply as a result of prohibiting an efficient rebate mechanism.

Conversely, where funds are purchased to underpin a product wrapper such as a life investment or structured product, the purchase is made on an institutional basis and rebates can be made to the institutional purchaser - the life company or bank. Such rebates can be passed on to the

ultimate investor in the form of cheaper units but could also be used to pay adviser charges – a facility not available to a fund manager if rebates of AMC to consumers is banned.

Additionally, since the units are on the balance sheet of the wrapper product provider, that provider has much more flexibility in buying and selling units and thereby releasing funds from within the product to facilitate adviser charging. Both aspects will make arranging adviser charging much less difficult for the wrapper product provider and distributor than for the fund manager and, for that reason, will make those products much more attractive. This will contribute to a continued bias toward life-wrapped and structured products in the investment market.

The effective favouring of life products and bank structured products in this way over more transparent equity and UCITS products seems incomprehensible and quite contrary to the aims of the RDR. Moreover, it is not a theoretical concern. We are already aware of providers issuing product information regarding pension products and retirement accounts that encourage the distributor to lead the consumer to believe that the cost of adviser charging is off-set by tax-reliefs inherent in the product.

Furthermore, we find inexplicable the FSA's conclusion that it no longer has a preference to ban payments in relation to non-advised business, particularly as it says it believes that it is desirable for there to be common standards for advised and non-advised business. The effect of this conclusion is that fund managers and platforms will have to maintain a rebate paying share class for non-advised business. They will also incur extra administrative costs in establishing whether the business is, or is not, non-advised.

**Q7: Do you agree with our proposal to extend the scope of ensuring all firms acting as nominee companies offer re-registration in specie?**

Yes. We note, however, that the proposed COB 6.1G.1 R is directed only at the firm from which the client wishes to transfer (N1), to the extent that the assets may lawfully be transferred. A further condition should be that the receiving firm (N2) is willing to accept the transfer.

In addition, although the rules cannot dictate which assets N2 must be prepared to hold for its customers, we believe N2 should be required to receive title to any asset that it is willing to hold.

In order for the proposed rules to work, the FSA should reconsider its use of the term "acting as a nominee company". Nominee company is defined in the Handbook Glossary as "a body corporate whose business consists solely of acting as a nominee holder of investments or other property". Such entities are in fact not authorised under the Financial Services and Market Act; rather, the FSA regulates the firms that use them for the purposes of holding client assets. Given this, we believe the term "acting as a nominee company", as proposed in COB 6.1G, is both ambiguous and unhelpful.

In addition, the overarching policy objective is to ensure that assets can be transferred away from a platform, which should include re-registration into the client's own name. The proposed

rules are, however, limited to transfers between firms that hold the assets on the client's behalf. We believe this is too narrow.

The proposed rules appear to introduce the concept of "acting as a registrar", which is unnecessary. By virtue of the Handbook Glossary, acting as a registrar limits the scope of the proposed COB 6.1G.2 to persons who maintain a register of unitholders of an authorised unit trust or OEIC. As such a person is not required to be authorised under the Act, the rule should be directed at the person who is responsible for that function. This concept already exists in COLL and should be re-used here. Indeed, we believe it would be far more logical and sensible to incorporate this particular provision within COLL 6.4.6R, which deals with the transfer of units.

Again, we would question the scope of proposed COB 6.1G.2, and suggest that the requirement be applied to re-registration more generally.

In order to address the above concerns, we would recommend amendments to the text of COB 6.1G, as follows:

#### **6.1G Re-registration of title to retail investment products**

Re-registration requests: firms holding on a client's behalf

- 6.1G.1 R If a *client* requests a *firm* that holds *units* on that *client's* behalf to transfer the title to those *units* to another *firm* that will hold the *units* on that *client's* behalf or to the *client*, and the *firm* may lawfully so transfer the title to those *units*, it must execute the *client's* request within a reasonable time.

Then, under COLL 6.4 (title and registers):

- 6.4.1 R (2) COLL 6.4.6B (Transfer of units - timeliness) and COLL 6.4.9 (Plan registers) also apply to the *ACD*, any other *director* and the *depository* of an *ICVC*.

...

#### **Transfer of units - timeliness**

- 6.4.6B R The *ACD* and any other *directors* of an *ICVC* or the *person* responsible for the *register* of an *AUT* should register an instrument of transfer within a reasonable time.

**Q8: Do you agree with our proposal that re-registration should be carried out in a reasonable time and do you have any feedback as to what might be reasonable for particular wrappers and assets?**

Yes. We believe there should be a general expectation in this respect, subject to the circumstances of a particular case.

For example, if N1 receives a request direct from the client to transfer to N2, it may need first to establish that N2 is willing to accept the transfer before it can execute the instruction. Where the request is received from N2, however, together with such client authority as N1 may require, N1 is in position to comply with the instruction immediately.

We would consider two business days as a reasonable timeframe within which to execute a transfer instruction (in the context of proposed COB 6.1G.1 R) that encompasses both the client authority and confirmation that N2 is willing to accept the transfer ("necessary authorities"). A firm should not be able to delay a transfer unduly in the absence of any necessary authority, so might in addition be expected to identify and request it within the same period, with the "timely transfer" period commencing as soon as it is received.

We believe a similar two-day period would be reasonable in relation to the re-registration of the underlying asset by the registrar under proposed COB 6.1G.2. Again, the registrar might also be expected to issue a request for any missing information or authority within the same period.

Where N1 is associated with an Authorised Fund Manager and maintains its client holding records in the form of a plan register in accordance with COLL 6.4.9R, the respective periods under the proposed COB 6.1G provisions might reasonably be expected to run concurrently.

**Q9: Do you agree that the new definition 'intermediate unitholder' incorporates all relevant firms?**

The new definition offered by the FSA does not capture all the intermediaries in the distribution chain. If the definition does not do this, then where there is more than one intermediary in the chain, investors will not necessarily receive key information from the fund, which is the intention of the requirement.

The fundamental issue is that few firms acting as "intermediate holders" will be entered in the register of holders in their own name. Instead, a firm (where it does not itself hold through an account with another intermediate holder) is more likely to hold the units in the name of a nominee company, which will not be an authorised person. We recommend, therefore that the definition be revised, as follows:

"a firm which holds *units* in a *non-UCITS retail scheme* or *UCITS scheme*, either directly as the registered *unitholder* or indirectly through a *nominee company* or another **intermediate unitholder** and which:..."

**Q10: Do you agree with our proposal to introduce a requirement for intermediate unitholders to pass on information provided by authorised fund managers to end investors?**

We agree with the intent of this proposal. However, we do not believe the drafting delivers that intent.

COB 14.4.1R fails to address an intermediary chain situation, as it is triggered only by receipt of information from the Authorised Fund Manager or depository. It should also be triggered by receipt of information from another intermediate holder with whom it holds an account.

Furthermore, the actual recipient of any information issued by the AFM or depositary is most likely to be a nominee company, which will not be an authorised person and, as such, will be beyond the reach of these provisions. We therefore recommend that the proposed COB 14.4.1R be revised as follows:

14.4.1 R (1) An *intermediate unitholder* which receives any of the notifications in (a) to (f) from an *authorised fund manager* or *depositary*, or an *intermediate unitholder* through which it holds units, must send...

...

(3) An *intermediate unitholder* which holds units through a *nominee company* must ensure that any notification in (1) that is received by the *nominee company* is forwarded to the *intermediate unitholder* without delay.

**Q10: Do you agree with our proposal to introduce a requirement for intermediate unitholders to pass on information provided by authorised fund managers to end investors?**

**Q11: Do you agree that we are allowing an appropriate level of flexibility by requiring intermediate unitholders to have appropriate systems and controls to either exercise voting rights on the instruction of investors, or to facilitate investors' exercising of rights?**

As we reported in our response to DP 10/2, IMA had previously relayed to the FSA concerns expressed by members that they were not easily able to communicate with end-investors where a platform is involved in the distribution chain. This issue was also highlighted in the IMA's review of issues arising from the credit crisis for authorised funds. We therefore agree with the intent of the proposal that consumers should have the same information and voting rights as if they had invested directly in the authorised funds.

However, it should be recognised that one of the appeals of investing through a platform is that the consumer is not subject to a deluge of information and can choose to be selective. We therefore suggest that consumers be allowed to "opt out" of full information service provision, provided the platform gives clear and regular warnings as to the potential consequences of this for the investor.

There is already a precedent for such an approach. For CTF and ISA customers, the rules/guidance oblige the providers to supply the Report and Accounts if the investor so elects. Many consumers, especially those who invest in ethical funds for example, wish their providers to cut down on the paper sent out and elect not to receive such information.

The FSA proposes that it would be acceptable to communicate by electronic means. This is welcome, but it is not a substitute for the ability of the consumer to opt out. Many providers do not have a record of their customers' email accounts. To conduct an exercise to obtain that information would be prohibitively expensive and unlikely to achieve any measure of success.

It is also the case that consumers are not likely to accept a rise in administration fees to receive information they do not require, or want.

**Q12: Do you agree with our proposal to require intermediate unitholders to provide aggregate information when requested by authorised fund managers?**

There is no commercial need or regulatory justification to require the supply of information regarding the identity of the end-investors and this information is not sought by our members as it would be of little or no value. However, our members do desire aggregate information about distribution channels and fund flows so that they can best serve the end-investor when designing, launching and marketing funds.

In the past the supply of distribution channel information by platforms has been mixed in delivery. Whilst this situation has been showing some improvement, and some key retail platforms now supply distribution channel information to the IMA, data provision remains inconsistent. A number of platforms remain unable, or unwilling, to supply this information. This has made it difficult for fund managers to understand the marketplace, the nature and drivers of demand, and the channels through which business is distributed. It also adds to difficulties in managing liquidity issues, which are the focus of the FSA's proposal.

Therefore, we agree with and welcome the FSA proposal to require intermediate unitholders (subject to our comments above regarding the definition of such unitholders) to provide aggregate information when requested to do so.

**Q13: Do you have any comments on the cost benefit analysis?**

In the absence of clarity over the rules and what is required regarding platforms, the industry is not able accurately to predict overall costs.

The FSA's cost estimate for the fund management industry seems to include only the costs of launching one additional share class per fund. It does not take account of the additional administrative burden of maintaining a legacy book and applying different processes for new business as well as execution-only. Such processes cannot be designed and implemented until these issues have been clarified.

Neither does the CBA mention the additional costs that will be incurred by the consumer in the likely higher cost of advice, together with the impact of a VAT liability.