

Guernsey's Financial Advice Standards (GFAS) – in response to UK's Retail Distribution Review (RDR)

Summary of Industry and Public Consultation Responses

March 2013

Summary of Consultation Details

A consultation document was released about the United Kingdom's Financial Services Authority's (FSA) Retail Distribution Review (RDR); its principles and proposals; how it may affect Guernsey and whether Guernsey should adopt a similar regime. The consultation was aimed at all interested stakeholders, financial services businesses, customers, consumers and other users of Guernsey's financial services industry.

The document was available on the States of Guernsey website, in paper form and was covered in the local media. The closing date was 2nd January 2013 and 14 responses to the consultation were received from the public, individuals, companies, trade bodies or organisations within the local finance industry.

Summary of responses

It was clear from the responses that the vast majority felt that Guernsey should adopt some form of RDR locally. Only one respondent suggested a more prudent approach for Guernsey of assessing the affect of the UK's RDR implementation before concluding on any options locally.

The highest number of responses were from companies within the local financial services industry (6 responses), including one Independent Financial Advisor (IFA) and a professional services firm. The rest of respondents were consumers (4); trade bodies responding on behalf of members (3) with another response from an independent compliance officer.

The responses to the specific questions are summarised later, however, not all respondents answered the specific questions posed in the consultation document but commented more generally about aspects of RDR.

Overall Summary

1. Most believed that a "lighter" version of RDR, which took the best of the UK's RDR, should be introduced locally on the grounds of:
 - a. Protecting and enhancing Guernsey's reputation.
 - b. Better value service for consumers, as advisers such as IFAs would be better educated and more professional with more transparent charging structures.
 - c. Protecting local business which, if RDR were not implemented, may go to other jurisdictions which have a form of RDR – e.g. other Crown Dependencies.
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- d. If RDR was not implemented Guernsey based investment managers / stockbrokers with UK clients may be prohibited from advising UK clients. If the UK client is an IFA network then RDR is needed or the IFA may not be able to appoint Guernsey Investment Manager.
2. Only one response favoured a “wait and see” approach rather than immediate implementation.
 3. A possible disadvantage of RDR banning commissions was highlighted by many, whereby customers may not use IFAs as they could be put off by up-front fees rather than the current perception of “free” advice which is spread out over many years – but which is actually paid for by commissions.
 4. A small minority thought it best to distinguish within the finance industry and introduce RDR for some areas and not others – e.g. retail only and not for professional clients.
 5. Most thought it best to introduce a similar RDR regime to other CDs to ensure consistency for group companies operating in Guernsey and other CDs and so that the CDs would be on a level playing field.
 6. Some larger operations, especially if they have UK clients or are part of a UK or CD group, are already implementing RDR compliant systems so the affect of local RDR is likely to be minimal to them.

Summary of consultation conclusions and the proposed implementation options for Guernsey – in light of consultation and other CD’s position on RDR

Introducing Guernsey’s Financial Advice Standards (GFAS)

Overall

1. C&E is proposing that “Guernsey’s Financial Advice Standards” (GFAS) be introduced in a response to UK’s RDR.
2. Implement the proposed changes in 2015.
3. Changes should only require rule changes by the GFSC, there should be no need for primary legislation.
4. The Commerce & Employment Board will write to the GFSC requesting that they implement the proposals and work with industry.

Increased professional standards:

1. General consensus was that minimal educational standards should be set to increase service levels to customers – standards should follow FSA and other CDs approach of FSA level 4. The Department agrees with this approach.
2. .
3. There was some inconsistency in responses in that some believed (as Jersey are proposing) that minimal educational requirements should be for retail customer businesses only (and not businesses that service more professional customers), but on balance it seems appropriate to require broadly equivalent to level 4 for all Guernsey businesses with retail clients.

Remuneration for investment advice

5. It was felt that abolishing commissions may mean less affluent investors will be disadvantaged as the market will not service them as they cannot afford upfront fees and IFAs may only focus on High Net Worth Individuals (HNWI). It may also lead to social exclusion by preventing less affluent individuals from having access to financial advice.
6. Some inconsistency in responses as some want commissions to be banned (Jersey approach) and others want firms to have the option of (1) full disclosure of commission but they can still receive commissions or (2) charge fees if the Advisor wants to (IOM approach). On balance the Department felt that allowing both commissions (but requiring full disclosure) and fees seems preferable as:
 - a. It is an improvement to the current system as it requires full disclosure of commissions.
 - b. It should be appropriate for both the domestic (more reliant on commissions) and international market and therefore should still allow potentially lower wealth clients to receive advice if they prefer to pay commissions.
 - c. Reduces the unnecessarily complicated need for a two tier approach of having RDR for domestic, but not international business.
7. Allowing disclosed commissions and fees is appropriate for all as some UK product providers will not now pay commissions thus all Guernsey entities will need a fee structure anyway.

Independent and restricted advice

1. Many concluded FSA definitions are not useful or suitable for the CDs – e.g. advice which is “whole of market” or “fully independent” is not possible for CD.
2. Thus it may be better to consider additional disclosure requirements to ensure clients are aware of limitations offered but consider adopting other terms (such as “tied” or “not-tied” or “whole of available market”).
3. The Department concluded that some categorisation of advice should be introduced and the actual categories should be a matter for the GSFC to determine in conjunction with industry.

Other – capital requirements

1. It was generally felt that FSA RDR requirements of £20k or 3 months reserves were unlikely to achieve the aim of ensuring a business has adequate resources to continue to service clients.
2. It would seem better to require each individual business to have appropriate Professional Indemnity Insurance (PII) in place.
3. Any PII requirements should not just be related to fee income / revenue but should be related to the risks of the business.

4. On balance the Department concluded that there should be no change to existing capital requirements.

Specific consultation questions

As identified earlier not all respondents answered the specific questions posed in the consultation document but commented more generally about aspects of RDR and included answers to questions in a more general response. The summary below focuses on those who did respond to the specific questions and also those who covered the main points in their general response.

General Comments on RDR in Guernsey

Question posed in the Consultation is in bold, followed by a summary of the response.

- 1. Question - General comments are invited on the overall view of a similar regime to RDR being adopted in Guernsey and whether it would be positive or not for Guernsey's financial services sector.**

Summary of response – A significant majority were in favour of some form of RDR as respondents felt that it would strengthen Guernsey's reputation, improve consumer protection and confidence. Only one preferred a "wait and see" approach.

- 2. Does your particular business need to meet UK RDR standards in order to be able to continue to serve UK clients?**

Not all respondents to the questions were from a business. However, most of the businesses that did answer this question, and particularly those who had UK clients and connections, felt that some form of RDR compliance would be beneficial in reaching this market.

- 3. Does your particular business intend to implement RDR compliant systems regardless of whether Guernsey chooses to implement RDR?**

Of those businesses that responded to this question many of the larger businesses which were part of group operations with a presence in other jurisdictions were already implementing RDR compliant systems, particularly in relation to educational requirements.

- 4. What are your views on the relative costs and benefits of RDR (or similar) in Guernsey?**

Again not all responses were from industry but those that were indicated that the benefits were likely to outweigh the inevitable (but many saw as manageable) costs which were seen by some as being worth the investment in an attempt to enhance the reputation of financial services.

Others saw that there were greater costs (and risk) of Guernsey not adopting RDR as business may shift from a potentially non-RDR compliant Guernsey to other competitor jurisdictions which adopt some form of RDR.

5. Does industry want RDR (or similar) to be adopted in Guernsey?

Most respondents were not speaking as general representatives of the finance industry, but from their individual (or business) point of view could see the potential positives outweighing the negatives. The industry representative groups felt that most of their industry did want some form of RDR adopting in Guernsey.

6. Do consumers of financial services want RDR (or similar) to be adopted in Guernsey?

The consumers who answered this question all wanted some form of RDR in Guernsey for the reasons already stated.

The business community believed that some form of RDR was positive for many of their consumers.

7. What do you think would be the impact on Guernsey if it was decided to do nothing in relation to RDR?

The message was repeated from earlier answers whereby it was felt that if Guernsey chose to do nothing in relation to RDR there would be reputational damage and Guernsey would be at a competitive disadvantage as the risk would be that international business in particular may move to a competitor RDR compliant jurisdiction.

8. Are there any elements of RDR which should / should not be adopted in Guernsey?

Many of the consumers who responded felt all parts of RDR should be adopted but did not go into the detail of any potential impacts on this. There seemed to be particularly strong views from the consumers in relation to raising educational standards, (reducing fees from IFAs – which is not part of RDR proposals but which gained some comment anyway) and banning commissions.

Industry was slightly more selective in its answering and the approach it suggested in relation to the main proposals under RDR with a minority advocating that all of RDR should be adopted and this view seemed to gravitate more from larger banking groups.

There was also a minority view that a two-tier system should be considered with retail business covered under RDR and professional business not covered.

A summary of the responses to each specific proposal under RDR is as follows:

- a) Almost total agreement on raising the educational standards (and where people commented on the specific level there was a consensus to raise it to FSA level 4).
- b) Slightly less agreement in relation to fees and commissions but the majority did favour some change with more in favour of allowing commissions but requiring them to be transparent through full disclosure while allowing and encouraging the charging of fees.
- c) Little agreement on the classification of advice with most believing that there should not be a classification of advice but if this topic was considered further then different categories of advice to those suggested under UK RDR would be more appropriate for Guernsey. Respondents suggested that having classification of advice were unduly complicated, misleading and unnecessary; very few firms could, in reality, ever genuinely offer whole of market, unrestricted or extensive independent advice.
- d) Some agreement in relation to capital requirements with the consensus being that capital requirements do not necessarily achieve what they intend to (which is to protect consumers) and if this topic was considered further a risk based approach with some requirements for adequate and minimal levels of Professional Indemnity Insurance (PII) (linked to risk and not turnover) seemed to be a better approach.

RDR Proposal - Increased Professional Standards for Investment Employees

9. Do you think it is appropriate for Guernsey to seek to raise the standards of qualification requirements for investment employees?

See 8 and 8 a) above.

10. If yes, what level should standards be raised to?

See 8 a) above

11. Do you have any other proposals which Guernsey could adopt which could address this issue?

There was some comment on this with a minority of industry responses suggesting that there could be a two-tier system whereby industry with retail clients should adhere to minimum educational standards and those with professional clients should not. However, most did not adhere to adopting this distinction.

RDR proposal – Remuneration for Investment Advice

12. Do you consider the RDR proposals to be reasonable in relation to changes regarding remuneration?

See 8 and 8 b) above

13. What alternatives would you suggest are more appropriate for Guernsey?

See 8 and 8 b) above

RDR proposal – Independent and Restricted Advice

14. Do you consider the two categories of advice and suggested ways that they are communicated to be appropriate for use in Guernsey?

See 8 and 8 c).

15. If not what classifications could be adopted in Guernsey?

See 8 c)

Other RDR proposals

16. Do you consider there is a need to require minimum financial requirements in Guernsey?

See 8 and 8 d)

17. If yes, what levels would you propose?

See 8 and 8 d)

Commerce and Employment Department's response to the industry Consultation on RDR

The Board of the Commerce and Employment Department are grateful to those who have taken the time to consider the proposals regarding RDR and send in their comments. The introduction of some form of RDR compliant regime in Guernsey was met with support from industry and consumers with most responding that a "lighter" version of RDR, which took the best of UK's RDR, should be introduced locally.

Most respondents felt that this approach would protect and enhance Guernsey's reputation; provide better value service from more professional advisers and a more transparent fee structure – all of which would benefit consumers. If RDR was not implemented it was generally felt that the greater risk is that some international and local business may go to other jurisdictions which have a form of RDR.

The Commerce & Employment Department will request that the GFSC take steps to implement the proposals which should only require rule changes and not primary or secondary legislation. If primary or secondary legislation is required then the Department will take steps to introduce such legislation. It is proposed that the introduction of Guernsey's regime should be effective from 2015.

The main proposals Commerce and Employment are making in light of the consultation are that Guernsey should introduce some changes shown below in order to ensure that Guernsey's financial services sector offers the very best service to consumers of financial products in Guernsey and to protect and enhance Guernsey's reputation as a leading International Financial Centre. The main proposals which the Department requests the GFSC to introduce are proposed to be:

1. Educational requirements: licensed financial services businesses which offer financial advice to retail clients should be broadly equivalent with FSA level 4.
2. Remuneration for providers: both commissions (but requiring full disclosure) and fees will be allowed.
3. Definition of financial advice and capital requirements: It is proposed that some categorisation of advice should be introduced and the actual categories should be a matter for the GSFC to determine in conjunction with industry

List of Respondents

There were a total of 14 respondents. The list of respondents has been not been published because not all respondents indicated if their identity could be disclosed.