
IFAs and Wealth Managers: Back to the Future?

An overview of the current state of the market and hot topics for underwriters and lawyers

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Back to the future?

2005 - 2014	2015 - 2016
Retail Distribution Review launched - 2006	Financial Advice Market Review launched - 2016
Concept of 'basic advice' introduced - 2005	Concept of 'guidance' being consulted upon - 2016
Pensions simplification A-Day - 2007	Pension freedoms - 2015
Risk profiling thematic review - 2011	Risk profiling thematic review - wealth firms and private banks - 2015
Refusal to adopt 15 year longstop date for FOS complaints - 2014	Refusal to adopt 15 year longstop date for FOS complaints - 2016
MiFID - 2007	MiFID II - 2016
Liquidity crisis : market volatility -2008	Brexit : market volatility - 2016

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The plan

- The current state of the market:
 - The impact of the Retail Distribution Review (“RDR”)
 - The Financial Advice Market Review 2016 (“FAMR”)
 - The ‘advice gap’ problem
 - Solutions: automated / robo-advice
 - Difficulties with ‘advice gap’ solutions
 - information, guidance or advice ?
 - what is the legal framework?

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The plan

- Round-up of other topical issues:
 - Pension transfers and insistent clients
 - Risk profiling and model portfolios
 - FCA Enforcement latest trends
- Conclusions: back to the future?

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Current state of the market

- Retail Distribution Review:
 - Launched in 2006
 - Majority of rules implemented by end of 2012
 - Desired outcomes:
 - Increased standards of professionalism
 - Industry engaged with consumers
 - More accessible market
 - Regulatory framework that does not inhibit innovation

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Current state of the market

- The RDR was successful, wasn't it?
 - Signs of increased professionalism
 - Reduction in product bias
 - Consumers shopping around more
 - Reduced numbers of IFAs?
 - Charges for retail investment products falling
 - Created opportunity for innovation

But...

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Current state of the market

- Total cost of advice has increased
- New business models: client segmentation
- Creation of ‘advice gap’
- Increased numbers of those:
 - not engaged with investment market
 - unwilling to pay for advice at realistic cost
 - seeking advice but firms unwilling to provide it

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Current state of the market

- Demand for lower cost simplified advice existed pre-RDR has not been resolved
- Advisers turning clients away due to affordability reasons
- Actual innovation to date has been limited

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Current state of the market

- FAMR identified more causes of the problem
 - Consumers willing to pay £250 for advice but average cost is £150 per hour
 - Increasing proportion of consumers buying products directly through platforms on non-advised basis
 - Only 27% agreed with the statement: “I am capable of sorting out my own finances without financial advice”
- FAMR indicated FCA commitment to solving the problems causing the advice gap

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Current state of the market

- FAMR: “It is important to expand access to high quality *guidance* services”
- Nervousness about providing ‘guidance’
- Clearer boundary between regulated advice and guidance is required
- Future professional indemnity exposures likely to be influenced by the efficacy of the market’s response to the FCA’s solutions to these problems

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Solutions to the advice gap

FAMR :

“Not everyone wants or needs a personal recommendation in respect of every decision, nor do they always need a comprehensive assessment of all of their financial circumstances and requirements. It is clear, though, that people would often like more support in understanding the options that are available to them. More can be done to create an environment in which firms can deliver tailored services which give consumers advice on a more limited basis or the guidance to instil consumers with the confidence to make their own decisions.”

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Solutions to the advice gap

- What solutions does FAMR recommend?
 1. Amend regulations and clarify terminology so that firms do not fear ‘guidance’ and limited advice models
 2. Develop clear framework to enable firms to deliver streamlined advice exploiting technology so that cost of face to face meetings are avoided - i.e. robo-advice

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Solutions to the advice gap

- Clear terminology
- FAMR proposes a binary framework: “guidance”, “advice with a personal recommendation”.
- Consulting on alternatives:

Guidance

Assisted self help

Tailored information

Financial help

Advice

Personal advice

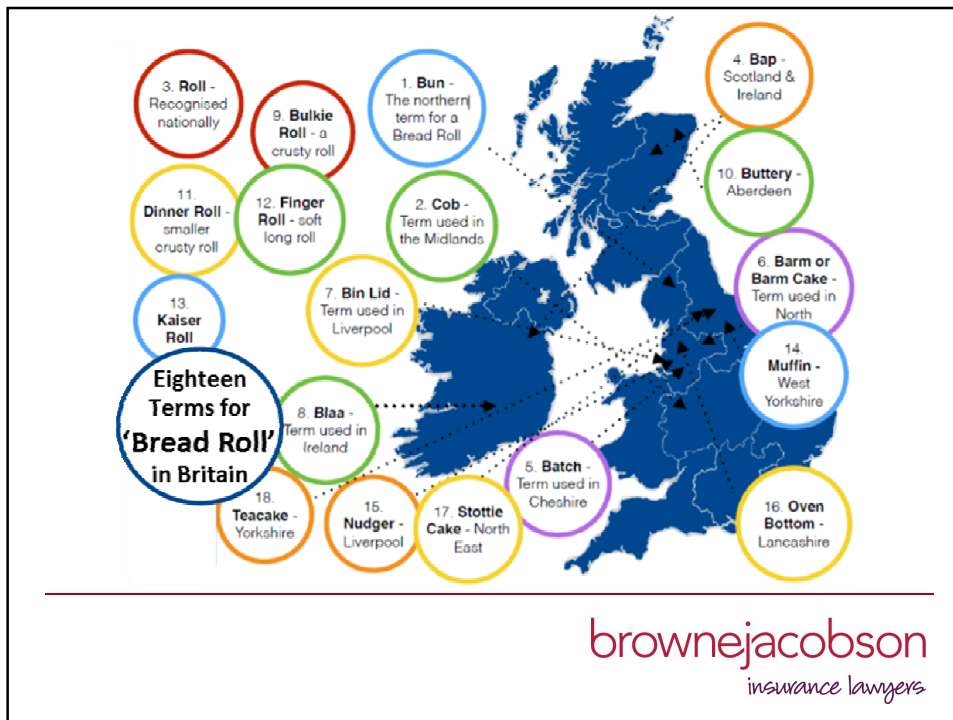
Regulated financial advice

Financial planning

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Solutions to the advice gap

- Designed to increase the number of advisers and providers willing to offer 'guidance', not just 'advice'
- Déjà vu? 'Basic advice' introduced in April 2005
- Will 'guidance' and information models represent a lower risk for firms and their insurers, or a minefield likely to lead to high claims frequency?

Advice, guidance or information?

- What is the relevant legal framework?
- Common law
 - Tort
 - Contract
- Statutory
 - FSMA 2000
 - Only 'private persons' have right of action
 - Conduct of Business Sourcebook (COBS)
 - Misrepresentation Act 1967

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Advice, guidance or information?

- Has any advice been given at all? Execution only?
Information?
- *Walker -v- Inter-Alliance Group* [2007] EWHC 1858
- *Rubenstein -v- HSBC* [2011] EWHC 2304 at 81-82:
 - What did the client ask for?
 - Does response contain evaluative commentary?
 - Is there an express disclaimer?
- *Thornbridge -v- Barclays Bank* [2015] EWHC 3430
 - Reluctance to elevate sales people to investment advisers status

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Advice, guidance or information?

- Advice - COBS 9.2.1
 - Take reasonable steps to ensure personal recommendation is suitable for the client
 - Obtain necessary information to be able to provide personal recommendation
 - Knowledge and experience
 - Financial situation
 - Investment objectives
- *Zika -v- Credit Suisse (UK) Ltd* [2013] EWCA Civ 14
- *Crestsign -v- NatWest* [2014] EWHC 3043

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Advice, guidance or information?

- Non-advised - COBS 10 or COBS 4.2
- COBS 10 applies if retail client and one of
 - Complex products (COBS 10.4.1)
 - Initiated by firm (direct offer financial promotion)
 - No warning about assessment of suitability
 - Conflict of interest
- Appropriateness test
- Obtain information about clients' knowledge and experience to assess their understanding of risks
- *Gabriel -v- Little* [2013] EWCA Civ 1513 (applying SAAMCO)

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Advice, guidance or information?

- *Bailey -v- Barclays Bank* [2014] EWHC 2882
 - COBS 9: concerned with suitability - whether the product or service is a 'good thing' for the client
 - COBS 10: concerned with appropriateness - whether the client has sufficient knowledge and experience to understand the risks involved

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Is robo-advice the future?

- Courts willing to recognise and enforce the boundary between advice and information in favour of financial service provider
 - *Springwell -v- JP Morgan Chase* [2010] EWCA Civ 1221
 - *Green -v- RBS* [2014] Bus LR 168 (CA)
 - *Crestsign -v- NatWest* [2014] EWHC 3043
 - *Thornbridge -v- Barclays Bank* [2015] EWHC 3430
- Get the contractual documentation correct and operate within it

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Is robo-advice the future?

- Key risks
 - Potential for error in automated tools
 - Risk of 'herding' if significant volumes of customers transact in the same way
 - Technical errors: who made the algorithm (do they have insurance?)
 - Inadequacies in contractual framework
- Greater clarity, hardening of the boundaries and dedicated support from FCA will reduce the risk
- Greater emphasis on s.5 (2) of FSMA

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Insistent clients

- What is an insistent client?
- FOS upheld 77% of complaints against IFAs where an insistent client process was used
- Enhanced value pension transfers
- FCA Thematic Review
- New pension freedoms

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Insistent clients

- Best practice
 - advice that is suitable for the individual client - i.e. normal advice process
 - it should be made clear to the client in writing that their preferred course of action is against advice
 - clear about what the risks of that course action are
 - explanation as to why insistent in clients own words

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Risk profiling and model portfolios

- 2011 FSA thematic review
- Of 11 tools reviewed, 9 had serious weaknesses
- The 2 tools that passed muster were not named - all 11 claimed they were one of the two!
- Model portfolios have benefits but forcing all clients into pre-determined model creates risk
- Expect to hear more from the FCA

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FCA Enforcement Trends

- Relevant whether or not policy includes representation cost cover
- Total penalties
 - 2008/9 = £28m
 - 2014/15 = £1.4bn
- Future:
 - emphasis on use of pre-emptive powers
 - personal accountability

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Back to the future

- Clarity of terminology
- Automated advice - rise of the machines?
- Return of banks and FIs to simplified advice for the mass market
- Market segmentation
- Improved conduct through regulatory focus on individual accountability
- Brexit volatility and recessionary pressures will expose misselling

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Questions?



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