Consultation response

December 2015

Call for Input on the Financial Advice Market Review (FAMR)

The CII welcomes the Government's efforts to make financial advice, in its broadest definition, accessible to all. The current alphabet soup of 'advice' terminology is bewildering to those working in the sector, never mind consumers trying to get their heads around these issues for the first time. Moreover, while the introduction of the Retail Distribution Review (RDR) made 'regulated' financial advice more robust, it is arguably beyond the needs of consumers with less complex requirements.

For the purposes of this consultation response, we are using the term 'advice' to mean any advice, recommendation or guidance given to a retail customer. This definition includes, but is not limited to, regulated advice (as defined in the FCA Handbook), as well as public financial guidance or other services that the customer may, rightly or wrongly, perceive as 'advice.'

If the Government and/or financial institutions are to make advice more accessible – by including, for example, new approaches and technology – they still need to ensure that the advice meets minimum standards, since this will engender public trust and confidence.

Drawing from its long experience as a professional body serving the pensions and long-term savings market, the CII last year proposed a standards model underpinning how pensions guidance could be built. We called this Standards, Training, Accreditation and Revalidation (STAR). It could form a confidence-building foundation from which the market could develop any existing and new 'advice' propositions:

- **Standards:** setting out what's expected of those firms giving advice or guidance, and what those individuals delivering it would be reasonably expected to know and perform;
- **Training:** to impart and verify the required individual knowledge and competence aspects of the standards;
- **Accreditation:** to confirm that the standards have been attained by organisations in their internal processes, and continue to be maintained; and
- **Revalidation:** to ensure that those individuals delivering these services are up to date with the latest developments, such as changes to investment and pensions policy, taxation and the benefits system.

Regardless of which service the adviser is giving, or the channel and label being used; if the advice is perceived as professional by the public, then it must be clear, transparent and, above all, robust with STAR is its foundation.

It is not our intention to try to design prescriptive guidance or advice models, or to express views on the relative merits of each. Instead, we wish to explore and understand how STAR could be applied in different broad scenarios. So we have asked consultancy EY to undertake a detailed analysis of possible guidance and advice scenarios that could stem from this review, and then set out how STAR might be applied. The EY report accompanies this consultation response.

Next Steps: the CII looks forward to working with HMT/FCA and the market to arrive at the right level of standards to support any emerging solutions, and help develop training, accreditation and revalidation solutions as required.

Our overall views of the reforms

The Chartered Insurance Institute (including the Personal Finance Society) welcomes the Government's efforts to make financial advice accessible to all. Whether it is regulated advice, a non-advised model, or 'guidance', the public must be confident that the service is capable of providing needed assistance to a reasonable standard.

With increased flexibility in the market, such as the pension freedoms and new products responding to a smaller welfare state, the need for advice has never been greater. We believe the Financial Advice Market Review offers a once in a generation opportunity to explore and support how advice can be given, and to unleash new thinking on how it could be given to those who need it.

What we mean by 'advice' in this response

We are using the term 'advice' to mean any advice, recommendation or guidance given to a retail customer. This definition is closer to what the public understand from the term, and as such is wider than the more prescriptive 'regulated advice' definition that those within the industry usually mean. Here then, 'advice' includes, but is not limited to, regulated advice (as defined in the FCA Handbook), as well as public financial guidance or other services that consumers may, rightly or wrongly, perceive as 'advice.'

Public trust and confidence must be at the heart of financial advice

The public has every right to be concerned about access to the advice sector, and the CII has done some work to explore the rationale behind this lack of confidence, and contributed to the efforts to improve it. FCA-regulated financial advice, whilst being high quality thanks to the RDR, is still beyond the means and desires of many.[1] Some might have more straightforward, less complex needs; and the range of advice descriptions currently covered by the regulations is bewildering to those familiar with the sector, never mind consumers trying to understand them for the first time.

Another major influence on confidence is the 'crisis of public trust' that exists, especially towards advice from any authoritative source.[2] This has resulted in an unprecedented rise in public scrutiny, and consistently high proportions of customers responding to surveys that they would rather self-advise, search the internet, or resort to the mainstream media, social media, and family and friends with their complex financial decisions. In our view, this potentially perpetuates the problem:[3]

- **Financial advice is inherently personal**: it is linked to the specific circumstances of the customer concerned, so what may have been suitable or useful for someone else may be wholly inappropriate for you.
- **Poor financial advice is not always immediately obvious**: unlike many other retail products and services, the nature of investment instruments means that what someone may have *perceived* as helpful advice at the time may turn out years or even decades later to have been quite the opposite. This makes redundant many of the social networking tools that consumers have come to rely upon in recent years such as word-of-mouth recommendations and user reviews.
- **Products can be deceptive even to people who *think* they are financially savvy**: people often report (and bemoan) the complexity of financial products. But studies repeatedly also reveal that those who *think* they are financially savvy are just as much at risk as those who are not. Even inveterate readers of the finance media may not be aware of the hidden risks in a product's design, or know what to do if their portfolio becomes exposed. In this age of on-tap information, access to professional advice is more important than ever.

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[1] See the Chartered Insurance Institute successive surveys on RDR implementation, the latest of which was *The RDR and consumers: the public's views towards the advice market*, Feb 2014, www.cii.co.uk/28904.

[2] See for example, The Chartered Insurance Institute, *What we talk about when we talk about trust: the future of trust in financial services*, Feb 2010. www.cii.co.uk/10116

[3] See for example, CII RDR consumer surveys (see note 1), Nick Hurman, "Listening to consumers: the future of financial distribution and advice," CII *Thinkpiece* no.6 (Aug 2008) www.cii.co.uk/10051; The Chartered Insurance Institute, *What consumers want: the public's views towards guaranteed guidance for retirement*, October 2014, www.cii.uk/32081

If professional advice is so important, the industry needs to find new ways of bringing it to the public – and in a way that engenders confidence. But improving accessibility by 'cutting corners' in safeguards potentially lays consumers open to a whole range of new risks, such as increased or opaque charges, or even outright scams. Regardless of the service offered, or the channel and label, the advice must be clear, transparent and above all robust.

Why are standards important?

We're not going to argue about the different advice models and the implications of regulation on commercial viability. Instead, the focus here is about the specific knowledge and capacity standards that people and organisations offering these services should be expected to meet.

In the context of financial advice, discussions about the 'knowledge and capacity of people and organisations' normally concern regulated investment advisers; and the standards themselves are couched in terms of qualification levels. However, this neglects an important component of the argument: qualifications are the *means* of delivering standards, not the standards themselves. In fact, the debate about standards can only begin by understanding:

- what services are being delivered;
- what knowledge is reasonably expected of the practitioners delivering those services (or involved in their creation); and only then
- how those people and organisations can demonstrate they meet these standards and keep them up to date.

The four-pointed STAR: Standards, Training, Accreditation and Revalidation

Drawing from its experience as a professional body serving the pensions and long-term savings market, the CII last year proposed a model underpinning how pensions guidance could be built. We think this could be applied to the wider issue of the FAMR advice scenarios. Delivering consumer protection that is appropriate to the service delivered can be described in terms of four principles: Standards, Training, Accreditation and Revalidation (STAR):

- **Standards:** setting out what is expected of those firms giving advice or guidance, and what those individuals delivering it would be reasonably expected to know and perform;
- **Training:** to impart and verify the required individual knowledge and competence aspects of the standards;
- **Accreditation:** to confirm that the standards have been attained by organisations in their internal processes, and continue to be maintained; and
- **Revalidation:** to ensure that those individuals delivering these services are up to date with the latest developments, such as changes to investment and pensions policy, taxation and the benefits system.

Why STAR delivers public trust and confidence: BEACON

STAR enables the range of models of advice or guidance to strike a three-way balance between being economically viable for firms in this sector to offer; being attractive and meaningful to customers; and assuring appropriate public protection. STAR could deliver that third element without the need for complex conduct regulation, since it would have the following characteristics (summarised here by the pneumonic BEACON):

- **Building block:** STAR must be part of the foundation of whatever models emerge if this review is going to deliver trust and confidence in the mass market;
- **Embedded:** STAR can become consistent across the different types of organisations, regardless of model. It applies to all those delivering such a service, be they advisory firms, other brokers, providers, guidance delivery bodies, or other parts of the sector or public organisations (alone or in partnership);
- **Accessible:** STAR can be clearly indicated to the public with kite marks or indicators. It would be relatively easy to promote and provide the information about what consumers should look for;

- **Chameleon-like:** rather than being a straitjacket that restricts the various scenarios and situations, STAR can be tailored and targeted. This means it can apply both outside and inside the sector, to public and private organisations alike, and to providers as well as intermediaries;
- **Oversight:** STAR could, in a relatively straightforward process, be overseen and managed by organisations that are independent of the financial services sector and with strong levels of public trust;
- **Now!** STAR would not be difficult to implement and would be seen as 'a quick win'. Many of the mechanisms and materials underpinning STAR could be rooted in resources that already exist, such as the training material created by the CII for Pension Wise, or the CII's material relating to its long-term savings initiative.

Applying STAR to the advice scenarios that could emerge from FAMR

It is not our intention in this submission to propose specific guidance and advice models to address the public's needs, or to express views on the relative merits of each. Instead, we wish to explore and understand how STAR could be applied in different broad scenarios. So we have asked consultancy EY to undertake a detailed analysis of possible guidance and advice scenarios that *could* stem from this review, and then set out how STAR could be applied. EY's findings are attached with this submission.

CII initiative: building trust and confidence in the wider pensions and long-term savings market

In addition to our public policy work responding to and implementing the Government's pensions reforms, the CII has also been engaging with leaders from the major pensions and long-term savings providers. We have formed a steering group to oversee the development of improved and more consistent standards at all levels within these businesses, particularly among customer-facing staff.

Our work has been informed by extensive consumer research and responds to the significant changes the sector has seen over recent years, not least the Government's pension reforms. We are now developing a 'public declaration' to which providers will commit, and this sets out a framework of professional standards that they will need to achieve voluntarily. We plan to launch this with several large providers early in 2016.

We believe this work will help to ensure that the sector develops the skill sets required to support the 'new normal' of the pension and long-term savings landscape.

Our responses to specific questions

Overview

Q1. Do people with protected characteristics under the Equalities Act 2010, or any consumers in vulnerable circumstances, have particular needs for financial advice or difficulty finding and obtaining that advice?

Yes. The advice models that FAMR seeks to develop must service all types of consumers, and our previous investigations show that more work needs to be done to consider their needs. In 2009, we published a report (with the thinktank Reform) on the need to actively engage young people aged 18-35.[4] In 2014, a task force we co-chaired with Age UK set out recommendations on the need to work better at reaching out to older consumers.[5] Earlier in 2015, we published a Thinkpiece with Scope about the barriers faced by consumers with disabilities in accessing financial

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[4] The Chartered Insurance Institute, *Money's too tight to mention: will the IPOD generation ever trust financial services?* October 2008. www.cii.co.uk/9904

[5] Age UK (with the Chartered Insurance Institute), *Financial resilience in later life*, June 2014 www.ageuk.org.uk/Documents/EN-GB/For-professionals/Consumer-issues/fsc_ageuk_financial_resilience_in_later_life_250614.pdf

products and services.[6] The recent report from the Financial Inclusion Commission points the way ahead as to how inclusiveness needs to be built into the whole process of product design and service delivery.

What do consumers need or want from financial advice

Q2. Do you have any thoughts on how different forms of financial advice could be categorised and described?

No, other than to reiterate there is a need to ensure they are described in a more meaningful way to the general public. Instead, we wish to explore and understand how STAR could be applied in different scenarios.

As explained, we have asked EY to sketch out different scenarios that could stem from the Financial Advice Market Review and consider how STAR could be tailored and delivered to promote public trust and confidence. Beyond regulated retail investment advice that already exists, those scenarios could be described as follows:

- **Technology enabled advice:** a number of different scenarios and permutations are applicable under this heading. Equally, many of the other scenarios highlighted in the report are, to greater or lesser degrees, underpinned by technology enablement. However, for the purposes of our STAR exercise, EY focused on three key themes:
  - **Full automation:** where an individual may be taken through an automated process, entering information where necessary, with the ultimate outcome being a recommendation or advice that is provided by technology. This scenario also includes the situation where an individual subscribes to automated guidance and advice that will be provided and implemented without the need for the customer's repeated explicit consent (i.e. through subscribing to a service, technology alters an individual's investment profile on a regular, ongoing basis without getting consent each time)
  - **Assisted advice:** this is where the digital tools helping consumers to identify the scope of their needs, and to create advice and guidance, are augmented (possibly at the customer's request) by an actual adviser. This could be applied in more complex cases, typically in relation to a specific need (i.e. life insurance or retirement planning) and could be self-service or advised
  - **Guided Advice:** includes remote advice delivered over the phone or video. This also includes omni-channel advice where the consumer's direct interaction with a practitioner becomes part of the process, or where an adviser becomes ultimately responsible for signing off the service provided.
- **Focused advice:** anyone wanting to operate in such a way could choose to focus on a very specific part of a customer's needs, in much the same way as a mortgage adviser does currently in a bank or building society. The scope of the assessment and advice on offer is very limited and would follow a pre-determined process.
- **Public financial guidance:** this topic of the parallel HM Treasury consultation could be delivered through public bodies such as The Pensions Advisory Service or Citizens Advice, and involve a hand-off of complex cases to focused advisers.
- **Assisted non-advised:** a scenario which focuses on helping consumers make better, more informed decisions about their financial needs, without providing any specific advice or recommendations. Although it is out of scope of regulated advice requirements (under both MiFID and Regulated Activities Order definitions) because it does not provide advice or recommendations, it can still be *perceived* as advice by the public. The Assisted Non Advised scenario provides consumers with accurate, relevant and timely information, and helps them navigate the often complex process involved in understanding their financial needs and the way(s) of fulfilling them. We think this is, potentially, an area for consumer detriment if the right safeguards are not put into place.

[6] Teresa Perchard, "How can people with disabilities get a better deal from the insurance market?" CII *Thinkpiece* 115 (April 2015). www.cii.co.uk/35446

Q3. What comments do you have on consumer demand for professional financial advice?

Q4. Do you have any comments or evidence on the level of demand for advice from sources other than professional financial advisers?

In 2011, 2013 and 2014, we surveyed consumers on the extent to which they receive financial advice.[7] Across all three years, we asked respondents who said they self-advise to rank the sources of information they are most likely to use. We found that financial assistance websites were the top choice: 46% overall ranked this first, and 27% put it second. It received the leading mean rating by a considerable margin. The Money Advice Service (MAS) was the second preferred choice and had the next most favourable mean rating, but this was because it ranked high as third or fourth choice. Newspapers and magazines ranked third overall, sharing a place with family and friends, but scored very high as second or third choices. Women put family and friends as their second preferred choice, and at a considerable margin ahead of the MAS. One key point is the importance of future, as opposed to current, demand based on higher public trust.

Q5. Do you have any comments or evidence on the types of financial needs for which consumers may seek advice?

Advice in different forms could be available to consumers across the financial spectrum, and depending on the stage they are at in taking decisions. People with fairly straightforward needs require assistance on general product or service purchases, or a type of 'helpful and independent friend' service to verify the merits of decisions they are about to take.

As the needs become more complex, people require a more in-depth and personalised assistance - one that has an element of judgment included about certain aspects (e.g. investment attitudes). Our recent research into the pension freedoms indicates that decisions like these might involve the customer going through multiple stages in their thought process. These are: initial fact-finding, engagement, and final decision, and each stage has specific information, guidance and advice needs.

	Initial fact-finding stage	Engagement stage
Needs:	Much earlier engagement by Government including a very simple 'Introduction to your pension options' highlighting the key principles to help frame personal circumstances. Use simple graphics (e.g. flowcharts) to aid understanding of the process and eliminate irrelevant information	Relevant information, answers to specific questions
Expectations:	Ideally led from an impartial (official) source, in simple language, concise and focused on what's important	*Qualified* advice or guidance, relevant to personal situation
Desired Benefits:	Being safeguarded from falling prey to non-impartial providers and/or overlooking better options through lack of knowledge	The ability to weigh the advantages and risks of different options
Desired outcome:	To be 'armed with information' to look into the detail of their own personal situation AND approach less impartial organisations e.g. providers	Being able to make an informed decision; awareness of the key risks involved

By the final decision stage, we think there is little or no need for further information, so there is little evidence that consumers will take further advice at the sort of mass market wealth levels we analysed in respect of the pension freedoms. The large majority of consumers will communicate their decision to their existing and chosen provider.

Q6. Is the FCA Consumer Spotlight segmentation model useful for exploring consumers' advice needs?

Yes. A segmentation model would result in a more precise analysis of consumer demand. However, perhaps a focus on consumer behaviour rather than products would be more appropriate. Discussions with the FCA suggest this might need to be developed as the regulator has historically taken a product-orientated approach to its work.

[7] The Chartered Insurance Institute, *The RDR and consumers: the public's views towards the advice market*, 12 February 201 www.cii.co.uk/28904; *The RDR and consumers: a research report into consumer views on the financial advice regulatory reforms*, 18 Feb 2013 www.cii.co.uk/24504; and *The Money Advice Service, financial capability, and the Retail Distribution Review*, 1 June 2011 www.cii.co.uk/9990

Q7. Do you have any observations on the segments and whether any should be the subject of particular focus in the Review?

No, the segments provided in the FAMR consultation organised around life stages are quite useful. The key to engagement in the future will be linking interventions to consumers at a point relevant to them, in particular life stages (starting out, young family, mature family, etc) or life events (first job, first child, retirement, etc).

Q8. Do you have any comments or evidence on the impact that consumer wealth and income has on demand for advice?

While there will be a price element to demand for advice, it is clear that those on low incomes will need (and possibly want) a variety of services at key stages in their lives.

Q9. Do you have any comments or evidence on why consumers do not seek advice?

Yes, our research suggests significant demand-led factors have an impact upon consumers' approach to advice: inertia; over-confidence in their own abilities/those of their friends/family; lack of trust in the sector; belief that they do not have enough savings to warrant advice.

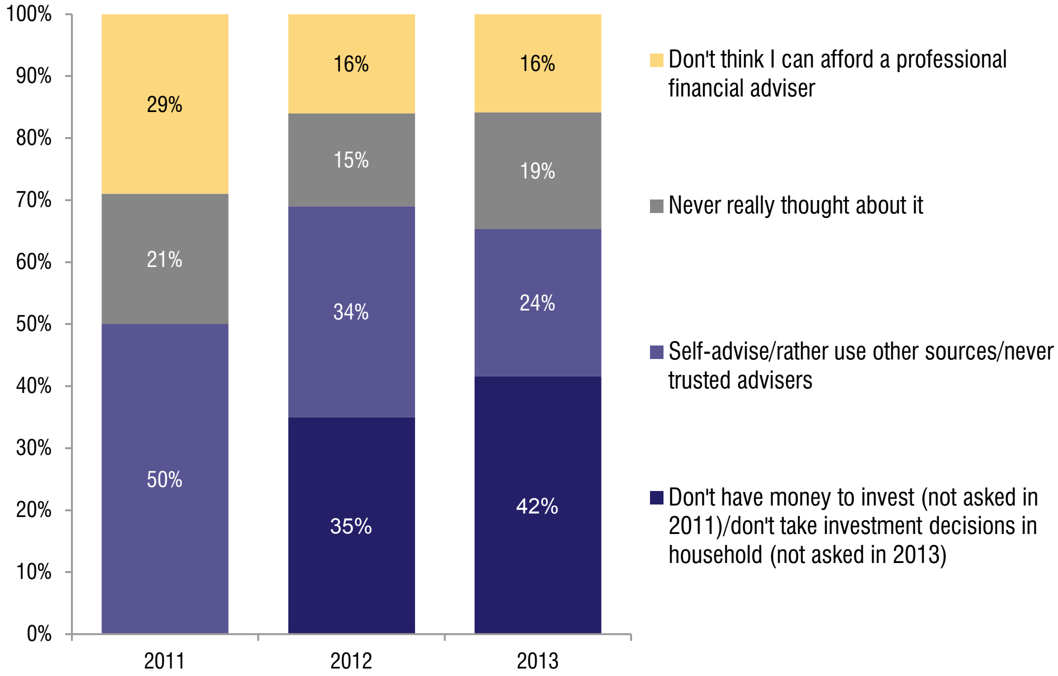
Research we carried out in 2011-2014 indicates a significant unmet demand by consumers who tend to self-advise or use other sources such as friends and family.[8] We found that of those who have not sought professional financial advice:

- 38% do not have the money to invest in 2014, almost the same as the 35% who said this in 2012.
- 4% took the new option that they do not take investment decisions in their household.
- 24% said they "would rather self-advise using other sources of information instead of professional financial advice". We deliberately combined the 2012 choices "don't need help investing, I do it myself", "never trusted financial advisers" and "rather use other sources of advice/information" into a single "self advise using other sources of information" because they are essentially the same choice, and it allows for a more robust data set. Overall it was 10% less than last year.
- 16% thought they could not afford a financial adviser, and this was consistent across every year of the research.
- Note: as with the 2013 survey, we filtered out those who answered that they do not have funds, or do not take investment decisions. They were not asked subsequent questions about awareness, willingness to take advice, trust and confidence, etc.
- Gender and age factors: self-advice: men are more confident in self-advising than women, though are not necessarily more competent: 30% of men said they would rather do this, whereas only 17% of women responded this way. 16% of those aged 25-34, compared to 45% aged 65+ "Never thought about receiving advice": younger adults were more likely to say this: 25% compared to only 9% aged 65+.

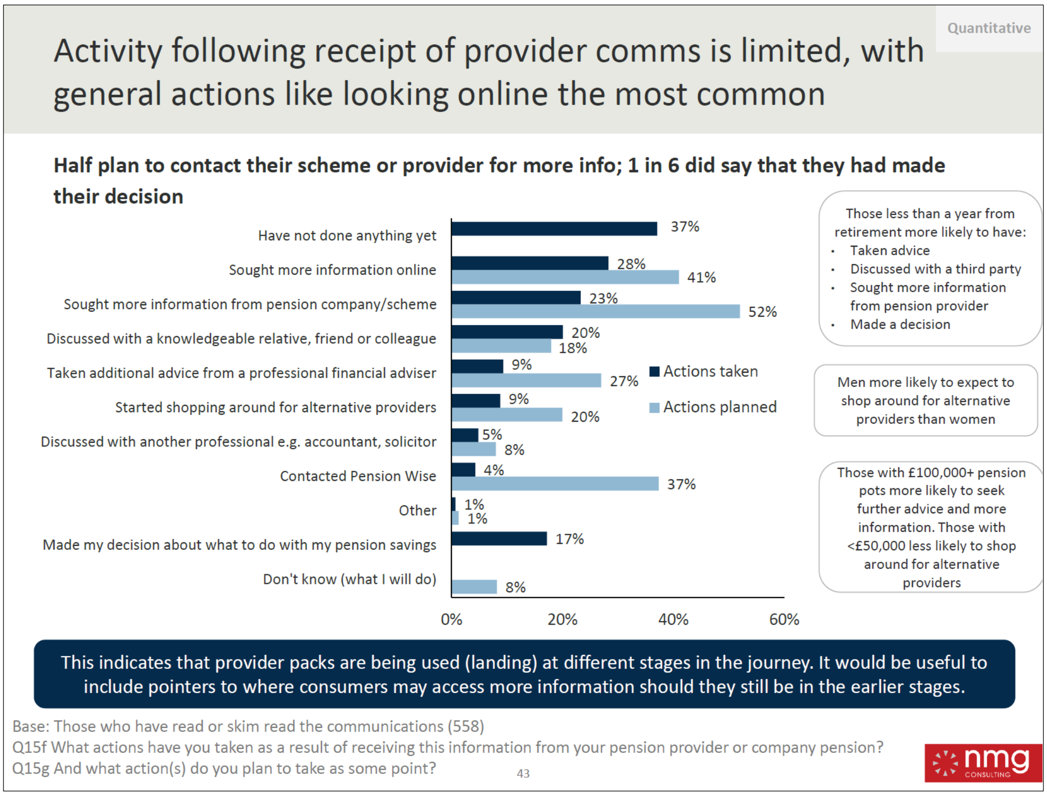
[8] See Note 7 above.

Reasons why consumers do not take financial advice

What is the main reason why you have never sought professional financial advice? (Base: 1,352)



More recent research we have conducted into the pension freedoms reveals a similar propensity towards finding information from a range of sources, with the media and financial information websites figuring strongly.[9]



[9] CII, follow up research into the pension freedoms undertaken in Sep 2015. Full details to be published in January 2016.

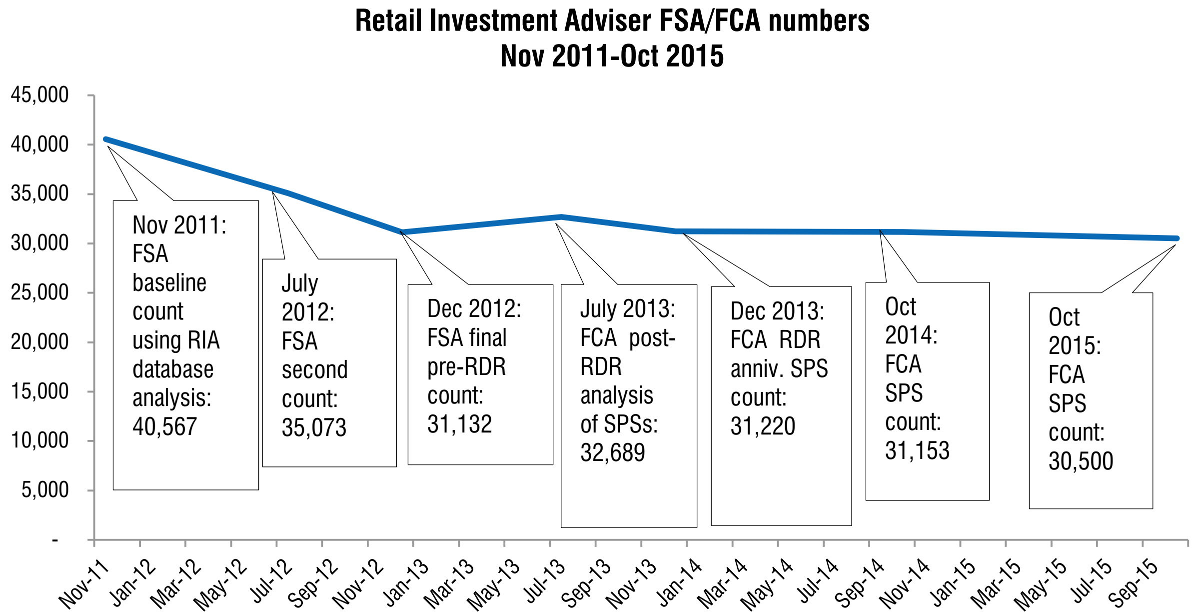
Where are the advice gaps?

Taking into account the findings of several pieces of research conducted over the past few years by organisations including the FCA, Citizens Advice and ourselves, we concur that there are both demand and supply elements affecting the access to and delivery of financial advice. We go into more detail about this below.

Q10. Do you have any information about the supply of financial advice that we should take into account in our review?

Our own view on the supply of advisers is based on the statistics of Statements of Professional Standing (SPSs) held by retail investment advisers (RIAs, of which about two-thirds are CII members). Since the introduction of that regime, and also detailed prior research for the FSA, this is by far the most robust indicator of adviser numbers.

We wish to point out that the 24,000 number quoted on p.15 of the FAMR call for input refers to the Association of Professional Financial Advisers data that only includes financial adviser staff *working in financial adviser firms*. Therefore, it ignores authorised RIAs in banks/building societies, wealth managers/stockbrokers, and discretionary investment managers.[10]



Based on the actual FSA/SPS numbers, RIAs have declined from an estimate of about 40,600 in November 2011 prior to the RDR introduction to 30,500 in October 2015. Although the overall drop across the period is significant (nearly 25%), the rate of decline arrested in December 2012 to a very gradual decrease of 2% overall between 2012-2015.

While it is still too early to say whether that pre-2012 reduction was sufficient to create any real consumer access issues (as some have argued), this two-phased process could well be explained by the following considerations:

1. **Plans to exit the market anyway:** a small proportion was intending to exit the market anyway, due to retirement for example. The FSA reported in 2011 that 5% of advisers planned to retire in the period up to December 2012, compared to less than 1% expecting to do so in their previous survey.

2. **Advice was previously secondary to main business:** some firms may have offered retail investment advice secondary to some other main business activity, and then decided to stop doing this ahead of the stiffer regulatory requirements. Arguably reducing this group was probably in the public's best interests anyway: successive FSA thematic

[10] The Association of Professional Financial Advisers' report The Financial Adviser Market in Numbers (edition 3.0), April 2015.

investigations into advice in various sub-sectors consistently highlighted problems with the advice given by such practitioners on the periphery of their main activity.

3. **Providers shedding direct sales forces**: a significant proportion may have been tied advisers working for providers such as banks and bancassurers, who left as a result of the providers eliminating their direct advice proposition altogether. Although some of these high-profile closures have been quietly replaced by another proposition, a large reduction in the direct adviser market has occurred. However:
   - one of the big issues that the RDR was trying to address was provider bias causing consumer detriment: of salespeople incentivised to sell unsuitable products. So arguably it is not surprising that some major providers have opted to exit this reputational risk source and move towards an entirely intermediated channel; moreover
   - anecdotal evidence suggests that many of these professionals have started their own businesses anyway, as independent or specialist restricted advisers.
4. **Ceasing trading due to professionalism requirements:** that leaves a proportion of advisers who genuinely did cease trading because they did not wish to meet the higher professional standards.

Finally, and this should surely be the fundamental position of any organisation involved or related to this sector: what is really in the public's best interests? More advisers with little or no consumer protection safeguards, some of which would probably have left the market anyway? Or 25% fewer advisers, but all with sufficient safeguards in place? Our view as a public interest body is the latter. As the real issue here is demand-led, please see our response to Q.13.

Q11. Do you have any comments or evidence about the recent shift away from sales based on professional advice, and the reasons for this shift?

See previous answers. The RDR has created a trend towards advice rather than a sales-led market.

Q12. Do you have any comments or evidence about the role of new and emerging technology in delivering advice?

We think financial technology could play a major role, and could drive down the costs for consumers. However, the technology must be subject to certain standards, training, accreditation and revalidation and we can go into more detail on how this could work. Clearly, technology will play an increasingly important role in both the lowering of cost and the increasing accessibility of advice. EY looked specifically at this area, including internet only as well as omni-channel services. We think technological innovation must take account of public trust to protect against, for example, consumers being hit with exorbitant charges or being guided towards more expensive services that they may not have paid for if they'd used other channels.

Q13. Do you have any comments on how we look at the economics of supplying advice?

We concur that some advisers have set minimum thresholds of investable assets, in a bid to target wealthier individuals and improve their profitability. However, we think this is a symptom of low mass market demand. We explained above that negative public confidence in the advice market combined with a low public understanding of the value of advice results in a low mass market demand. In those conditions, there is also no incentive to create new lower-cost solutions to serve that market. So instead, advisers focus and prioritise their business to serve the much more lucrative affluent market. If mass market demand were to increase, advisers would be incentivised to innovate to serve them, leading to a fall in charge levels and asset thresholds.

Q14. Do you have any comments on the different ways that firms do or could cover the cost of giving advice (through revenue generation or other means)? Do you have any evidence on the nature and levels of costs and revenues associated with different advice models?

This is a business model question best answered by firms themselves.

Q15. Which consumer segments are economic to serve given the cost of supplying advice?

In the current market conditions, more affluent customers with high investment levels are the most economic for advisers to target.

Q16. Do you have any comments on the barriers faced by firms providing advice?

This is a supply question best answered by firms themselves.

Q17. What do you understand to be an advice gap?

There are potentially a number of different factors influencing the low take-up of financial advice by the mass market. Whereas the label 'advice gap' is often used, we believe the factors here are more complex, and could actually be described as an education and awareness gap, and a savings gap. These gaps may apply individually or collectively to consumers at different stages of life, depending on a wide range of different factors. The key issue is around encouraging people to save more often and to understand the responsibilities and implications placed upon them.

As Europe Economics has identified in its report for the FCA on the post-RDR impact, the individuals falling into the advice gap can be placed into three groups:

- **The Unserved (the 'economic gap'):** those with financial assets to invest who are engaged with the market, and willing to pay fees for regulated advisers, but unable to find an adviser willing to serve them. The unserved may be regarded as individuals who are direct victims of the demand-led problems described in our response to Q.13 above. Although they have the assets and willingness to take up advice, no financial advisers are available for them.

According to a Towers Watson report, an advice gap does not exist among the unserved because the industry has enough active financial advisers to cover consumer demand. Based on numbers quoted in the report, there are approximately 30,000 advisers while the total number of consumers would amount to a need of about 25,000 advisers. However, the post-RDR environment has witnessed advisers increasing the minimum threshold of investable assets in a bid to target wealthier individuals and improve their business model. Although there may be enough advisers to serve any consumer with assets (and the willingness to pay the true cost of financial advice), the increased difficulty among those with less investible assets could lead to a consumer perception that they are left unserved.

- **The Unengaged (the 'education gap'):** those with financial assets to invest, but not engaged in the investment markets. The unengaged can be regarded as individuals who have fallen within an education gap. Inertia means that the individuals within this group do not invest and this is most likely to be overcome through education in the importance of investment and the different available channels for advice.

There is evidence, supported by the FCA Practitioner Panel, that the exit by many bank-based advisers following the implementation of the RDR meant there were less mid-market advisers that provided mass market access to advice. For this reason, the number of investors with £50,000–£100,000 has declined. There is certainly an opportunity here to develop propositions which this segment of the market desires.

- **The Unwilling (the 'confidence and trust gap'):** those with financial assets to invest and who are engaged with the market, but regard the fees of full regulated advice as too expensive or too high for the quality of service that they expect. Individuals such as these either pay for a cheaper alternative or prefer self-directed investments. The unwilling can be regarded as individuals who have fallen within the confidence and trust gap.

Adviser remuneration issues: a GfK survey showed that 34% (340,000 clients) of active investors who have taken advice from an independent financial adviser in the past five years have said they would "never consider paid-for advice". This marks a decrease of confidence among investors in the advice regime. Since the costs for financial advice have become more transparent following the RDR, consumers have decided not to take full regulated advice but instead to find cheaper alternatives or go directly to the product provider. Gross sales of financial products via financial advisers, wealth managers, and stockbrokers have declined from 50% of total sales in Q1 of 2010 to 36% in Q2 of 2014. In contrast, the gross value of direct sales increased from 35% in Q1 of 2010 to 55% in Q2 2014. This trend suggests that, as more investors have lost confidence in financial advisers, they have sought self-directed investment as an alternative that can provide better outcomes for its cost.

Separate research by Citizens Advice in October 2015, in addition to research conducted by the Financial Services Consumer Panel in March 2012, suggests that there may be at least five gaps in the advice market. They are classified as follows:

- **The Affordable Advice Gap:** this gap affects consumers who are willing to pay for advice but not at current prices.
- **The Free Advice Gap:** this gap affects people who want advice but are unable to pay for it.
- **The Awareness and Referral Gap:** this gap affects people who are not aware that advice exists, or where to get that advice.
- **The Preventative Advice Gap:** consumers affected are those who would benefit from having money advice as a preventative measure. It is the result of the failure of public financial guidance to respond to the challenges that people face during phases for their lives.
- **The Engagement / Persuasion Gap:** this gap affects people who need to be actively engaged and persuaded that getting money advice is a good use of their time and that there are experts who can better assist them with handling their money.

The analysis of the different groups does not explain 'what' the solutions should be. The three groups do not neatly fall into their own respective demographic segment, but instead pervade across a number of segments. The difficulty with resolving the advice gap is that each demographic segment has its own particular needs and responds to distribution channels differently. It is for this reason that there isn't a 'one size fits all' solution.

We have also done our own research on this subject, with the last survey in 2014, which is consistent with these findings. This suggests that adviser charging is not the main deterrent for people with the money to invest, but rather:

- Inertia;
- Apathy and lack of confidence in the adviser market, probably fuelled by media coverage of the mis-selling scandals; and
- Lack of understanding of not just their own knowledge but also of their limitations, and those of their so-called 'trusted' advice substitutes such as friends/family and the internet.

Q18. To what extent does a lack of demand for advice reflect an advice gap?

The above analysis of the different groups that constitute the advice gap would help address 'how' the scenarios should operate to resolve the advice gap. To reduce the unserved, the existing adequate supply of financial advisers should be maintained and supplemented with alternative mechanisms to cater for the needs of different consumers. This should be coupled with increased education, awareness and improvement of consumer perception. To reduce the unengaged, more education should be openly accessible to the public and initiatives should focus on spreading awareness of the different available channels to acquire financial advice. To reduce the unwilling to pay, initiatives should focus on reinforcing consumer confidence and trust in the current advice regime and reassuring the market that the advice would give a pay-off that is worth the fees charged.

Q19. Where do you consider there to be advice gaps?

There needs to be an intermediate provision between public financial guidance and full financial advice. There is currently very limited provision to help consumers with specific aspects of their finances, such as what decumulation option to proceed with. There is no middle ground between public financial guidance that cannot make specific product or service recommendations, and regulated financial advice that must investigate all aspects of the customer's circumstances.

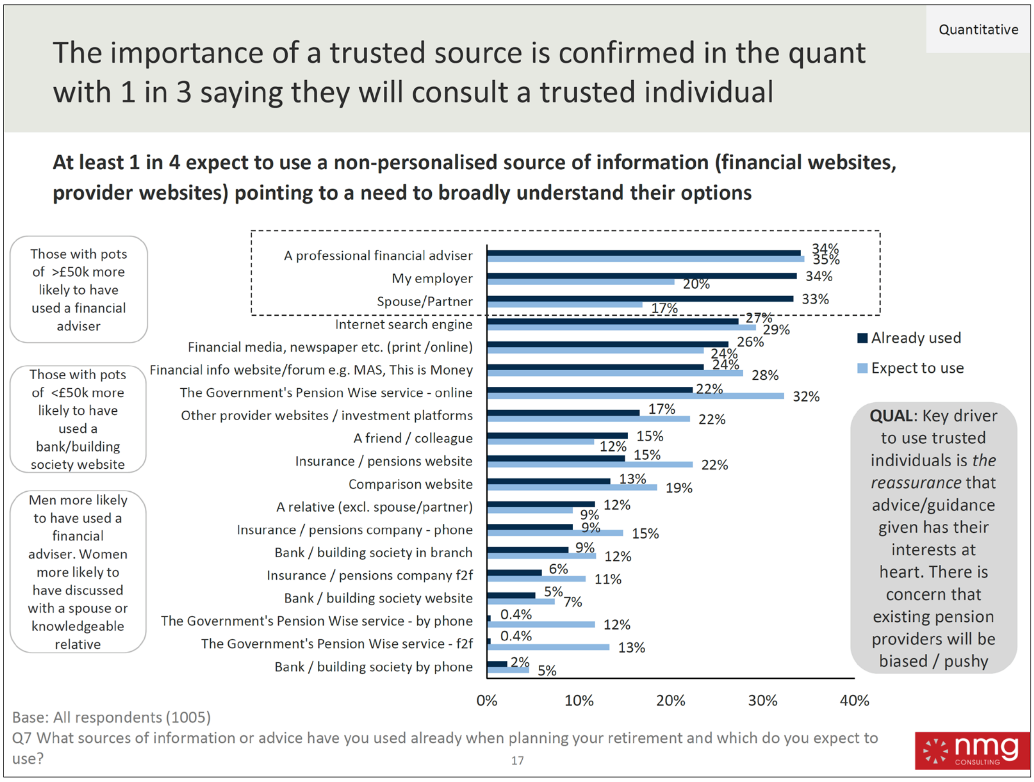
Q20. Do you have any evidence to support the existence of these gaps?

Our research suggests that significant demand-led factors have an impact upon consumers' approach to advice: inertia, over-confidence in their own abilities/those of their friends/family, lack of trust in the sector, a belief that they do not have enough savings to warrant advice.

Research we carried out in 2011-2014 indicates a significant unmet demand by consumers who tend to self-advise or use other sources such as friends and family. We found that of those who have not sought professional financial advice:

- 38% do not have the money to invest, almost the same as the 35% who said this in 2012.
- 4% took the new option that they do not take investment decisions in their household.
- 24% said they "would rather self-advise using other sources of information instead of professional financial advice". We deliberately combined the 2012 choices "don't need help investing, I do it myself", "never trusted financial advisers" and "rather use other sources of advice/information" into a single "self advise using other sources of information" because they are essentially the same choice, and it allows for a more robust data set. Overall it was 10% less than last year.
- 16% thought they could not afford a financial adviser, and this was consistent across years.
- Note: as with the 2013 survey, we filtered out those who answered that they do not have funds, or do not take investment decisions. They were not asked subsequent questions about awareness, willingness to take advice, trust and confidence, etc.
- Gender and age factors: self-advice: men are more confident in self-advising than women, though are not necessarily more competent: 30% of men said they would rather do this, whereas only 17% of women responded this way. 16% of aged 25-34, compared to 45% aged 65+. "Never thought about receiving advice": younger adults were more likely to say this: 25% compared to only 9% aged 65+.

Our more recent research, into the pension freedoms, reveals a similar propensity towards finding information from a range of sources, with the media and financial information websites figuring strongly.



Slide from CII 2015 pension freedoms research

Q21. Which advice gaps are most important for the Review to address?

See our response to Q1.

Q22. Do you agree we should focus our initial work on advice in relation to investing, saving into a pension and taking an income in retirement?

Yes, we concur that these are the areas where the public's interests are best served. However, we also think this scope should be extended to protection insurance and equity release mortgages.

Q23. Do you agree we should focus our initial work on consumers with some money but without significant wealth? What exact income/wealth thresholds should we use to determine which consumers we will focus on?

It is not for the CII to comment on these thresholds. However, we do think there is a danger of focusing on 'wealth' groups and neglecting the behaviour of certain specific groups. The FCA's segmentation analysis was quite sophisticated in that it moved beyond consumer inertia thinking and understood that certain types of consumers adopt certain approaches based on their interests and specific circumstances.

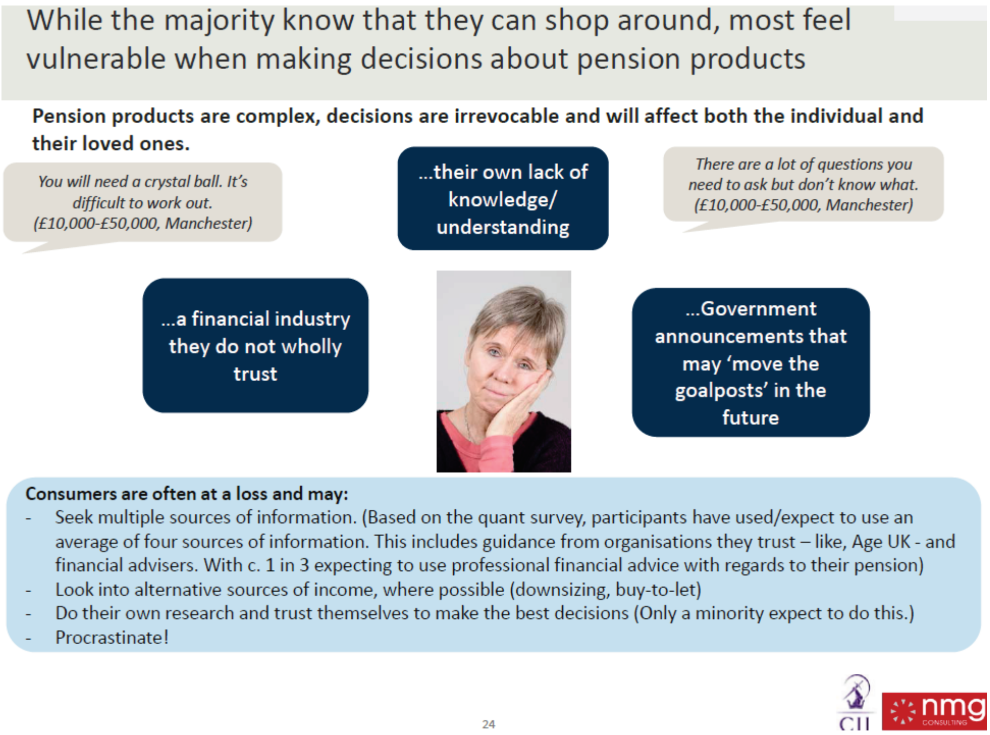
What options are there to close the advice gap?

Q24. Are there aspects of the current regulatory framework that could be simplified so that it is better understood and achieves its objectives in a more proportionate manner?

The current regulatory framework is appropriate for full financial advice on retail investment products following the Retail Distribution Review. We do not believe these should be amended. However, provisions should be created for additional, simpler advice models that would meet the needs of all types of consumers, while at the same time meeting minimum standards of training and competence. As an appendix to this consultation response, we have developed some proposals suited to possible new models.

Q26. What can be learned from previous initiatives to improve consumer engagement with financial services?

There is strong historical evidence suggesting that much of consumer inertia or limited action is down to either a lack of information or mistrust, or both. In our research into the pension freedoms in 2014, we found a considerable degree of confusion and anxiety about what consumers could do next.



Q29. To what extent might the different types of safe harbour described above help address the advice gap through the increased incentive to supply advice?

While it is not our position to comment on how safe harbour could or could not work in practice, our view is that any solution must have the consumer's best interests at its heart, and be underpinned by standards, training, accreditation and revalidation. The attached report by EY suggests how this could be applied.

Q31. What steps could be taken to ensure that a safe harbour includes an appropriate level of consumer protection?

Such is the current uncertainty within the market place, with regards to liability and the potential for future recourse, that some parties are reticent about offering simple solutions to those with simple needs. This is due to a belief that the modest fees that can realistically be charged do not outweigh the potential future costs, driven through recourse. There is considerable scope for reform here, and the attached EY report sets out how safeguards such as STAR could be put in place to support consumer protection.

Q36. Do you have any comments on the extent to which firms are able to provide consistent automated advice at low cost? Are you aware of any examples of this, either in the UK or other jurisdictions?

While we cannot comment on the ability of firms to give automated advice, or how to deliver this in an economic manner, we believe that STAR should be applied to ensure the best outcome.

Q37. What steps could we take to address any barriers to digital innovation and aid the development of automated advice models?

One barrier could be consumer concerns or even scepticism towards technology-led solutions. We think STAR could be applied to this and the attached report details how this could look.

Q38. What do you consider to be the main consumer considerations relating to automated advice?

We recognise a number of risks arising from financial technology solutions, which must all be addressed:

- **The service has to be clearly understood:** by the customer and not prone to any misinterpretations. Therefore the service has to be directed at the right type of customer.
- **Data security:** the details about the customer's financial circumstances and subject to data protection law.
- **Robustness of the algorithms underpinning the technology:** the recommendations given must be financially sound and be in the customer's best interests. Whatever the level of human intervention that the technology entails, there has to be an element of judgment involved in recommending specific courses of action to the customer. Whether the algorithms are able to make specific recommendation to specific customers, or whether they use comparison techniques based on similar customers, the principles behind them must be sound from a financial perspective.
- **Liability of recommendations given:** how can it be ensured that the technology provides the correct advice, and who takes responsibility for any liability? Is it the software provider of any solution, the firm offering the product, or is it the person who writes the algorithm?
- **Transparency of pricing and information:** customers need to be confident that the prices of products and services transacted over this channel are competitive with those purchased through other means. Costs, prices and charges must be clearly transparent and itemised so as to be comparable across channels. The customer should clearly see that the product's 'robo-advice price' is similar to the 'non-advised price', and if not, why not.

In order for this scenario to work, there will need to be a number of key principles established;

- relevant and personalised: any advice must take into account the consumer's specific personal circumstances
- clearly defined scope (e.g. consideration of debt, long-term care, etc.) and purpose (e.g. helping customers understand what the implications of their decisions might be)
- roles and responsibilities are clearly defined and understood
- in a Guided advice model, the customer accepts responsibility regarding the suitability of their choices.

We believe that automated advice could be one way to allow consumers to receive some sort of assistance. However, those providing such a service must meet STAR principles, and we have analysed how this could be delivered.

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Contact:

Laurence Baxter
Head of Policy & Research
020 7417 4783   laurence.baxter@cii.co.uk