“The Consumer Investments Market”

Submission by the Transparency Task Force, December 15th 2020

About the Transparency Task Force; a Certified Social Enterprise.

The mission of the Transparency Task Force is to promote ongoing reform of the financial sector, so that it serves society better. Our vision is to build a highly respected international institution that helps to ensure consumers are treated fairly by the financial sector. The primary beneficiaries of our work will be consumers; but the sector itself will also benefit through improved market conduct and increased trust in the services it provides.

Our objective is to carry out a broad range of activities that help to drive positive, progressive and purposeful finance reform, such as:

- Building a collaborative, campaigning community; the larger it is the more influence it can have in driving the change that is needed
- Raising awareness of issues; so that society better understands the problems that exist in the financial sector and how they can be dealt with
- Engaging with people who can make change happen; because through such dialogue we can influence thinking, policy making and market conduct

Much of our focus is on rebuilding trustworthiness and confidence in financial services. To make this possible we are busy developing a framework for finance reform which we describe as a “whole system solution for a whole-system problem” as described in our recently published book. We believe that there is merit in being constructively critical of financial regulators, where it is clear there is scope for improvement and where we are able to offer sensible solutions to the issues we see.

For further information about the Transparency Task Force see here.

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Q1: Have we prioritised the right issues and questions? Are there other things you think we should be looking at?

We believe the FCA is at risk of overlooking the need for fundamental changes to the regulatory framework, without which the consumer investments market will continue to be full of flaws, causing ongoing consumer detriment and the continued collapse of confidence in the system as a whole.

To use an analogy, it is as if the FCA is concerning itself with the architecture of a house without giving due concern to ensuring the property is built on solid foundations. Whilst of course the design blueprint as a whole is important, however good the design it is at risk of serious failure if the foundations are not fit for purpose.

We shall therefore initially turn attention to what we see to be the prerequisites for firm foundations in our regulatory framework:

#1: There needs to be a strategic overhaul of the basic approach to regulation through the introduction of a legally enforceable duty of care to consumers.

#2: There needs to be a total rethink of the requirements around professional indemnity insurance, whereby it should become the individual that must be covered, not the firm the individual works for. Finance professionals must be held personally accountable, whereas at the moment individual regulated advisers, IFAs and FCA company directors are not held personally responsible for fraudulent misrepresentation, only the company that is regulated is, which means that the FOS and FSCS operate to compensate victims of fraud after the event. Nothing is in place to protect the consumer before the event and very often nothing is done to the perpetrators.

#3: The "Sophisticated Investor" regime needs to be abolished because it has been abused so much that it lacks credibility as a regulatory instrument, as shown in this example, which highlights the abuse of restricted investor exemptions by unauthorised scammers.

#4: To counter the issue that we don't have 'regulated products' in the UK but instead specified /designated investments (with exemptions), regulated activities (with exemptions) & financial promotions (with exemptions) through a patchwork of FSMA, the RAO & the FPO which means even the FCA and FSCS have to use advice from external counsel (and even judicial review) to work out what is 'regulated', we must follow the far better US system whereby all investments/products must be registered with filings before they can be promoted or sold to the public. If those filings include details of the receiving agent for funds invested the register gives a watertight 'white list' for banks, trustees etc to use to screen out scams etc.

#5: The regulatory perimeter must be substantially extended such that virtually all products are regulated; and if ever there is uncertainty as to whether the product is regulated or not,

the default must be that the benefit of the doubt be given to the consumer. Furthermore, regulated advisers must be banned from dealing with any unregulated products; a breach to be a criminal offence.

#6: All financial regulators must report into a given Minister for Financial Regulation, to increase transparency and accountability and avoid conflicts of interest at the Treasury

#7: The FCA's Financial Services Consumer Panel should be managed and led such that it operates as an effective panel representing the interests of the consumer and given full permissions to constructively and openly criticise the FCA.

#8: There needs to be crystal clear clarity in relation to what exactly is meant by terms such as advice and guidance, with sufficient attention being paid to ensuring the consumer is fully aware of the regulatory status of, and levels of accountability applied to, the organisations and individuals that he/she is dealing with.

#9: All intermediaries must take a professional oath; akin to the medical profession's hippocratic oath, whereby the privilege to advise people on financial matters is granted only to those that are willing to expose themselves to significant consequences in the event of their having been shown to have acted unprofessionally, such as a highly-publicised lifetime ban from the sector.

#10: The Senior Managers Certification regime must be applied as intended; i.e. it must actually be applied.

#11: The FCA must pass full responsibility for ensuring that the advertising of financial products and services is not misleading to the Advertising Standards Authority, who have a track record of doing that kind of work well; whereas the FCA most definitely do not

#12: The power of deterrent must be fully harnessed through the FCA becoming known for making good use of its powers, resulting in swift, effective and robust enforcement, especially in cases involving fraud, where the FCA is often seen to act in a rather timid and unduly risk-averse manner. This is a good recent example of the need for the FCA to act in a more timely manner. Prompt and assertive enforcement must becomes the rule, not the exception:

Having made our opening remarks in relation to the need for fundamental improvements to the fundamentals, we shall return to them throughout this response where relevant to do so.

Regarding the consultation questions themselves, we believe that the included questions are all relevant to the subject, but that key areas of inquiry have been omitted, even beyond the fundamental issues already addressed.

Our response to this consultation, and we suspect many others', draws heavily on a number of themes that have been raised extensively by campaigners and consumer representatives - ourselves included - over a number of years, not least in consultations such as this. These issues include:

- Tackling asymmetries of knowledge and information;
- Achieving transparency on charges;
- Improving alignment of economic incentives;
- Promoting competition;
- Reducing switching costs;
- Eliminating exit fees;
- Addressing the advice gap;
- Updating or removing the high net worth/sophisticated/professional investor exemptions;
- The need for financial promotions to be accurate;

- The lack of clarity regarding the regulatory perimeter; and of which products are within and outside of scope for the FSCS;
- Improving consumers' access to redress from those who cause them loss, both regulated individuals and the regulator;
- The need to deal fairly with legacy cases of industry misconduct and regulatory failure;
- Introducing a duty of care of regulated individuals , firms and the regulator to users of financial services;
- Reducing the prevalence of scams;
- Transforming the proactivity of the FCA in performing its statutory duties

The elephant in the room is that the FCA has long been aware of the groundswell of opinion on these topics but has persistently resisted implementing the changes that have been advocated. Every time a new Chief Executive is appointed, meaningful reform is promised and consultations are launched, but when it comes to changes that are resisted by influential bad actors in the industry, grounds are always found for kicking the can down the road.

This problem is not merely historic. As recently as November 2020 the FCA announced that it would be terminating its work on what it misleadingly described as 'platform exit fees' (in fact the original consultation dealt with exit fees from a much wider range of financial services providers) - on the grounds that 'at least two major platforms' had eliminated such charges. The same statement admitted to yet another delay to its long overdue consultation on the principle of a duty of care, which was the single biggest ask from campaigners and consumer representatives in response to the mission review launched by Andrew Bailey following his appointment, some five and a half years ago, and something that we suspect certain industry stakeholders are very keen to avoid.

Given all the foregoing, and in anticipation of what are likely to be two highly critical External Reviews into the FCA's handling of failed consumer investment products[1], we believe that any consultation that aims materially to improve how this market works for consumers must also address the following questions:

- Is the Financial Conduct Authority fit for purpose?
- If not, how should it be reformed; or what kind of organisation/s should replace it?
- What governance and transparency regime needs to be in place to make a reformed FCA or its successor/s sufficiently accountable to politicians, consumers and wider society and less vulnerable to producer-interest influence from the industry, theTreasury and the Bank of England?

Some of these questions are touched on by the second phase of HM Treasury's Future Regulatory Framework consultation, though even that fails to acknowledge the extent to which what it calls 'the FSMA model' needs radical reinvention due to the apparent longstanding problems with the culture, incentives and governance of the FCA.

[1] The Connaught Income Fund Series 1 and London Capital and Finance

It may be that the optimum solution is the creation of some hybrid of an Australia-style Royal Commission and a Truth and Reconciliation Commission, in which the focus is on cooperatively admitting to past shortcomings and establishing best practice for the future and trading financial redress for past victims for some degree of leniency for perpetrators.

Q2: Are there other underlying issues which have an impact on the consumer experience in this market that you think we should consider? What are they and how do you think they affect consumers?

We believe there is a material risk that the UK economy as a whole is suffering from a sizable deadweight loss arising from a lack of confidence in its financial services sector, and in particular, in the consumer investments market.

Campaigners and regulators alike often focus on asymmetries of knowledge and information, but seldom of confidence. If consumers lack confidence about participating in a market, they may rationally choose not to do so. Consequences may include:

- People of working age failing to make sufficient savings for retirement; be that through pensions or other arrangements. Consequences:
  - Them having to stay in the workplace longer than they'd like
  - Job vacancies not being freed up for younger people
  - The affected individuals suffering poor standards of living in old age
  - The state having to support more elderly people through pension credits
- Older people under-occupying family homes, perhaps at least in part because they perceive property to be a safer haven than financial investments, potentially because they've been scared or personally affected by scams and mis sold products. Consequences:
  - Them suffering income shortfalls and having to pay to upkeep larger properties
  - Families having to pay more for less spacious housing, due to a lack of availability
- The financial services industry being smaller and less profitable than would otherwise be the case. Consequences:
  - High-value jobs not being created that would otherwise exist
  - The Treasury being deprived of payroll taxes those employees would have generated and of stamp duty and VAT on the financial transactions and professional services forfeit
  - Shareholders in financial services firms enjoying greater profits, and the Treasury participating in these through taxes levied on dividends and capital gains

It is therefore our view that a better functioning consumer investments market would benefit the industry, government and wider society, and not only consumers. Losses would be small, and would be concentrated on 'bad actors' - dishonest or complacent industry participants and insufficiently effective regulators. Sadly, those incumbents may enjoy greater lobbying power than the far more numerous and financially significant beneficiaries, which may help to explain why there seems to be such resistance to material change.

Q3: What role could or should 'just in time' consumer education play in helping consumers make more effective investment decisions?

We accept that the referenced meta study concluded that the forms of financial education evaluated may not have been appropriate to the needs of consumers in managing their capital, but we dispute the implication that there is no role for improving financial literacy in building consumer capacity to make better decisions about consumer investments.

It is self-evident that, for example, an experienced investment banker is likely to have more capacity to understand retail financial services products, even those wholly unrelated to his or her sector, than a random citizen, as a result of having absorbed concepts and terminology during his or her career; in the same way, we can see a role for the timely acquisition of path-dependent knowledge by consumers as they pass through different life stages at which financial education becomes necessary to help avoid risk of loss and achieve targeted gains, but at which it is not always provided at present.

Such financial life stages could include:

- Getting a first job
- Starting a family
- Changing jobs
- Buying a home
- Retiring etc

Furthermore, as well as significant life stages, there are other times when timely education could be helpful, such as:

- Auto-enrolment into, or declining to participate, in a workplace pension scheme;
- Opening a Lifetime ISA, ISA, SIPP or share dealing account;
- Investing a material sum of money via any platform in an investment trust, unit trust, ETF or other collective investment vehicle;
- Engaging in leveraged trading, buying futures, short positions, spreads, derivatives or other complex products;
- Transferring out of or consolidating a workplace pension;
- Putting a pension into any kind of drawdown;
- Buying an annuity

In our response to the Work and Pensions Committee Consultation on Protecting Pension Savers we recommended extending the remit of The Pensions Advisory Service and Pension Wise so their services are available to those under 50, as well as above it, and giving consideration to making consulting with it mandatory before certain key events, such as transferring out of a defined benefit pension plan.

We believe that these services, rebranded, or similar schemes, could be used to help empower consumers to achieve appropriate levels of financial literacy before passing through life stages of the kinds listed above. Ahead of some events, there might be a requirement to complete a free online

exercise[2], in others also to pass it. For larger transactions and more momentous decisions, there might be a requirement to receive in-person advice from either an independent financial adviser or one of these services[3]. And at each point of contact, further resources should be provided, combined with prompts to take advantage of them. Note that great care must be taken to ensure that education is not being given by somebody who is simply a conflicted sales person - or providers whose agencies they hold - product-interest has no part to play in consumer education.

There is a big difference between the solution described above and that outlined in paragraph 2.8 of the consultation document. The latter appears to equate just-in-time 'consumer education' with behavioural prompting. This is not a satisfactory substitute for financial literacy, especially when provided by a party with an economic interest in shaping a consumer's knowledge, and at a time when he or she is about to decide whether or not to buy that firm's product. Whilst we are supportive of the idea that better-informed and better-educated consumers are more likely to make better decisions, especially if any input provided is timely, we wish to highlight that there are many risks if that education is not delivered correctly. We are surprised to note that the FCA considers such a proposal worthy of consideration, given the obvious potential for conflicts of interest and suboptimal treatment of consumers to arise. We are therefore concerned that perhaps the FCA has confused financial education with choice architecture.

Q4: What more can we do to help the market offer a range of products and services that meet straightforward investment needs?

[2] The benefit of providing financial education online is that the marginal cost of doing so is zero

[3] This raises two obvious questions: who should meet the marginal cost of delivering this service; and whether it should be restricted to financial coaching (the provision of which is unregulated) or financial advice (a regulated activity)

The question implies that there may be a shortfall in the provision of 'products and services that meet straightforward investment needs.' We are not convinced that this is the case; the market includes a wide range of products that are likely to meet almost all types of consumer need, including some very low-cost Index Funds, ETFs and platforms. If the FCA has undertaken any market research that leads it to believe that it has identified unmet needs, it should place the same in the public domain and enter into a productive dialogue with the industry and with genuine consumer advocates about how those gaps might be filled or why demand cannot be met.

We suspect it may be more accurate to say that 'the needs of many consumers for straightforward investment products are unmet' and that this is happening at least in part because consumers lack the necessary information and confidence. This may be the result of a combination of a lack of financial literacy (which could be addressed by the measures proposed in response to questions 2 and 3), shortcomings in how those products are communicated and fear caused by legitimate concerns about the risk of being exposed to underperformance or scams.

A market that functions well is not just one that provides consumers with a choice of products that together meet most consumer needs; it is one in which consumers also feel able to transact, and one in which they do so. The FCA's competition objective recognises this, requiring it promote effective competition in financial services in a manner that has regard to five factors [our italics]:

(a) the needs of different consumers who use or may use those services, including their need for *information that enables them to make informed choices*,
(b) the *ease with which consumers* who may wish to use those services, including consumers in areas affected by social or economic deprivation, *can access them*,
(c) the *ease with which consumers who obtain those services can change the person from whom they obtain them*,
(d) the ease with which new entrants can enter the market, and
(e) how far competition is encouraging innovation.

Improving the quality of information available to consumers, simplifying the journeys by which they identify and invest in specific products and reducing switching costs would together make it easier for them to choose products that would suit their needs. Giving them the confidence to go ahead and commit their savings is likely also to require improvements to the regulatory and compensatory regime so they feel that downside risk has been reduced.

We touch on these themes throughout this response document.

Q5: Could clearer, consistent labelling of investment products help consumers make effective decisions? Please provide examples where this approach has/has not been successful.

Yes. Paragraph 3.4 of the consultation document hints at a suitable approach. Taking the example of food, while some consumers with a background in nutrition might find some value in being told how

much sugar is in a product, for most this information is unusable because they don't know how much they require, how much is in the rest of their diet that day, or how much might risk harming them. A traffic light system is a proxy by which the food industry and government have decided to provide that utility: not only is it colour-coded but it also shows a proportion of the recommended daily intake, and a quantum for the most nutritionally literate.

The principle of a rating system works also in high-value, non-consumable goods, including those where life is at immediate risk if the wrong purchase decision is made. Ever since 1998, all recreational boats sold in the EU and EEA must conform to the Recreational Craft Directive. This requires manufacturers to label almost all new and secondhand vessels in one of four categories, according to the states of water that they can safely handle:

- Class A - the boat may safely navigate any waters
- Class B - the boat is limited to offshore navigation. (Winds up to Force 8 & waves up to 4 metres)
- Class C - the boat is limited to inshore (coastal) navigation. (Winds up to Force 6 & waves up to 2 metres)
- Class D - the boat is limited to rivers, canals and small lakes. (Winds up to Force 4 & waves up to 0.5 metres)

We believe it would be inappropriate for us, in this document, to propose a labelling or traffic light system for financial services products. Rather, such a scheme should be developed by the regulator, genuine consumer advocates and the industry, based on cooperative sharing of relevant market and behavioural research and inputs from those who have developed successful schemes for other sectors.

We note that this consultation exercise is taking place against a background of the UK leaving the transitional arrangements it passed into on exiting its membership of the European Union, a time when it is expected no longer to be bound by requirements placed upon it by the EU. Among those was the obligation for firms offering consumer investments to provide a Key Investor Information Document (KIID) for each product.

The KIID has been widely, and we believe justifiably, criticised. In particular the Risk Indicator and Performance Scenarios are required to contain information that asset managers would themselves consider to be misleading and unrealistic *ex ante*, and which all too often turn out to be so *ex post*. The need to replace it with something better is pressing.

Likewise, and especially when dealing with products intended to build confidence among consumers who might otherwise be reluctant to invest, transparency over fees is crucial. Disclosure needs to be provided in a clear and meaningful way - there is a significant difference between unhelpful data that the average person won't understand and decision-enabling, clear and intelligible information presented in such a way that it aids comparability. This is another long standing issue that the regulator ought by now to have resolved.

Q6: What are the potential risks and benefits of standardised labelling requirements for consumer investments?

The single biggest risk is of repeating the KIID mistake by compelling the industry to provide misleading information to consumers. The opportunity is to get it right this time. The benefit is that consumers will find it easier to compare products and become more confident to invest.

Q7: What are the barriers to firms providing simple investment products for consumers?

The fact that simple investment products do exist means that there are not insurmountable barriers to their creation. The fact that many people who might benefit from such products are either not investing at all or using more complex (and probably more expensive) investment products would suggest that there are some obstacles to their launch and adoption.

Obstacles to the launch of more simple investment products might include:

- Difficulty or impossibility of creating product differentiation ('one FTSE100 cap-weighted ETF is much like any other')
- The need to achieve significant scale if, as is often the case, a simple product also carries very low charges
- The fact that regulatory charges are likely to represent a significant and unavoidable proportion of the costs incurred in operating a simple, low-cost product
- The possibility that a more complex product could deliver higher returns for consumers and the providing firm alike

Obstacles to the adoption of simple investment products may include some people:

- Not knowing that they exist
- Not understanding terms and costs
- Knowing that they exist but not knowing that the products are suited to their needs or how to invest in them
- Being tempted to invest in them but being deterred from doing so by fear of financial loss caused by poor management, misconduct, regulatory failure or some combination of the three
- Believing, whether rightly or wrongly, that more complex investment products are better suited to their objectives and risk appetite or are intrinsically superior (for instance, by delivering superior performance)

We touch on the themes identified in these bullet points throughout our response.

Q8: Do you think financial guidance can help consumers make effective investment decisions? Why?

We think it is unfortunate that the FCA launched this consultation before publishing the research referred to in paragraph 3.6. Having access to that research would have helped respondents in addressing a number of the questions raised in this exercise, this one included.

We believe it is important to distinguish between five types of activity:

- *Financial education*: helping a consumer to improve their understanding of the key concepts involved in personal finance. Unregulated
- *Financial coaching*: helping a consumer to improve their understanding of his or her own personal goals, priorities and behaviours as they relate to personal finance. Unregulated
- *Financial planning:* helping a consumer to plan his or her goals, and model the financial architecture to support them without personal recommendation. Unregulated.
- *Financial guidance*: helping a consumer identify their options and narrow down their choices but without recommending a particular product or course of action and without straying into giving personalised advice. Unclear whether regulated or unregulated - it is not regulated under FSMA but the regulatory boundary is not always clear
- *Financial advice*: recommending that a consumer purchases specific products, makes specific asset allocations and so on, based on a thorough understanding of their individual circumstances, goals and risk appetite. Regulated

We have reservations about the concept of financial guidance. If it's deemed to be unregulated because no personal advice is given, we see there to be a huge opportunity for both (i) the well-intentioned but incapable. And (ii) scammers to set themselves up as financial guides and direct consumers toward unsuitable product categories, whether in good faith or bad.

The key is to regulate financial guidance where it is completed in preparation for a regulated activity, whether that be a product purchase (or sale) by the customer, completed with the guidance provider or elsewhere, related or unrelated to the source of the guidance. Financial guidance that is truly generic or educational IS unregulated.

And if it's deemed to be regulated then it is difficult to see how it can be acceptable to steer a client toward a narrowed-down set of options without a competent fact-find, the presence of which would imply the same process, cost base and outputs as regulated financial advice. It is not deemed to be regulated.

If guidance is generic, then no products are sold. They may of course be purchased elsewhere by the customer, unrelated to the source of the guidance. There should not be any fees (much less additional fees) applied to the purchase as no advice was provided.

It is surely preferable to empower consumers to make good decisions for themselves, or to direct those who do not wish to do so to the IFA community.

Q9: What are the barriers to firms providing financial guidance services?

The main barrier is that firms struggle to make money out of guidance unless it ends in a product sale.

This renders the guidance route as less attractive to market participants commercially.

The FCA has decreed that guidance is general or generic, unless it is delivered as part of the preparation for a regulated activity. Guidance delivered as part of the preparation for a regulated activity is a regulated activity. Advice is personal. Guidance that is general or generic carries no risk for the giver. Advice does, so there is significant difference in the cost - and rewards - of delivering both.

Generic advice is a term the FCA uses to refer to something that is advice rather than mere information but which is not regulated because, although it relates to investments, it is not about the merits of buying or selling a particular investment. PERF 17.5

The FAMR report described streamlined advice as:
'A term used to collectively describe advisory services (such as focused and simplified advice) that provide a personal recommendation that is limited to one or more of a client's specific needs. The service does not involve analysis of the client's circumstances that are not directly relevant to those needs.'

Effectively, a decision tree is a tool that helps deliver advice, which may be generic advice or a personal recommendation, depending on the questions asked and the solution presented to the customer.

Hence, the use of a decision tree does not, in itself, determine whether a firm is providing regulated advice or not.

Guiding someone through a decision tree where they make their own decisions, would not normally be seen as 'advising on investments'.

Whether the advice is regulated depends if a personal recommendation is being provided in relation to a specific investment. The FCA stressed two key considerations: Is the decision tree process limited to assisting a person to make their own choice of product? Or is the decision tree process likely to be perceived by the customer as assisting them to make their own choice of product, taking into account the features that the customer regards as important?

For it not to constitute a personal recommendation, the decision tree and, where relevant, the person asking the question it contains, would need to avoid making any judgement or assessment that would result in a single product or a list of products being identified as suitable for a customer, whether as a result of information that the customer provides or otherwise.

However, it is entirely reasonable for a decision tree to provide a range of options.

Guiding resulting in intermediation carries the same costs and risks as advised sales. For many this renders this approach of providing guidance only as ‘Not worth it’.

Non-intermediating guidance carries far lower costs and risks, and rewards.

Trees created by product-interest industry - sell products, therefore these are advised, and appropriately regulated.

Trees created by product-interest of the Treasury to sell "accumulation", for increased tax revenues and reduced strain on the benefits system. For example, small pots generated by Auto-Enrolment simply deprive future generations from means tested benefits in retirement - should be treated as guidance in preparation for a regulated activity.

Trees need to be created by independent people who put client best-interest first, with a wall placed between guidance and regulated activity. Unless that guidance is part of the regulated activity as explained earlier.

Q10: Do you think straightforward financial advice can help consumers make effective investment decisions?

By Straightforward the FCA means paying off debts, saving for a rainy day, and purchasing an ISA.

Every product arranged by an IFA has an ongoing liability (for the client's lifetime) , even if the product is considered a one off. Therefore advisers are attracted to products that- with the client's agreement - provide an ongoing income to contribute to the ongoing costs of service. .

The fact that FCA data indicates that 94 percent of IFAs provide ongoing services does not mean that only six percent offer one-off (many do both), or that 94 percent of IFAs' revenues come from the former. It would be useful to understand the absolute and trend data in the provision of advice split between ongoing and one-off. Also, no data has been provided on how charging is split between *ad valorem* ('x% of investable assets'), interval-based ('£x per annum') or activity-based ('£x to advise on investing the proceeds of an inheritance') models. It would be helpful if the FCA could publish such data.

We would guess - and hope - that the trend is toward the growth of one-off advice and activity-based fees at the expense of ongoing advice and *ad valorem* and interval-based charging. Advice is more affordable, and perhaps crucially, *feels* more affordable to the end user, when it is purchased for a fixed fee at a time when a specific decision point has been reached. Depending on the specifics of a client's circumstances, goals, risk appetite and asset allocation, there may be merit in arranging periodic subsequent reviews - but for many clients, ongoing charging represents poor value for money. Unless of course the client puts value on having his portfolio reviewed and rebalanced regularly in line with his risk profile; notwithstanding that daily rebalancing is included in various low-cost funds for OCF of just 0.22%.

Furthermore, if our goal is to be the empowerment of consumers to make appropriate financial decisions for themselves, IFAs should recognise that their role includes elements of *financial education* and *financial coaching*, as well as *financial advice*. Over-reliance on a charging model based on ongoing fees could create a perverse incentive to deliver suboptimal services for clients in those advisers who are not client focused. However, for IFAs who don't handle client money, all investment decisions should be made by the client following detailed research and recommendation.

This business model offers the potential to break the link between purchasing advice and buying financial products. Currently, for most people, an adviser provides a set of recommendations, and is also the conduit to the execution of those ideas, and their ongoing monitoring and servicing, and rebalancing in line with the client's risk profile and change of circumstances. Under a segregated model, the IFA provides generic recommendations, then leaves the client to carry them out, undertaking his/her own research to find suitable funds to suit the generic recommendations. There is no servicing or portfolio rebalancing, unless the client can undertake those him/herself, which for the unskilled may lead to a suboptimal result.

This may also weaken an important route to market for scammers, who either pose as IFAs or corrupt genuine ones with the offer of undeclared commissions. It should be understood that if the IFA's recommendations are personal to the client (as distinct from generic advice) then the fact that the IFA lets the client arrange the purchase of products him/herself does not exclude the IFA from ongoing liability for the suitability, and regular review of the products recommended. Such an arrangement would not be breaking the link between advice and buying financial products.

So in conclusion, despite there being incomplete information provided on this topic, it would seem to be a desirable goal that IFAs be encouraged to provide what the FCA terms straightforward financial advice. Doing so might help reduce the advice gap, which is large, and widely held to be growing. However, as there is no difference between advice and straightforward advice for the IFA it should be understood that what the FCA terms straightforward advice does not mean one off advice. If it's an ISA it carries ongoing responsibility for the IFA.

Q11: What are the barriers to firms providing simple advice models?

There are none for IFA firms , provided clients are prepared to pay the fees. As all regulated advice provided by an adviser carries the same responsibilities and liabilities, it follows that it should carry the same rewards. So advisers do not differentiate between simple regulated advice and any other regulated advice.

While some consumers might imagine the advice needed is a ‘once off’ affair, the regulator requires the regulated adviser to accept responsibility for that advice for the remainder of the client’s lifetime and effect PI insurance to cover any potential claims at any point in the future. Hence the regulated adviser is not keen on providing advice that does not provide a matching ongoing income.

Q12: Should the redress model for simple advice be any different to standard financial advice? If yes, please explain.

No. We believe every regulated adviser should be civilly liable for losses caused to clients by negligent or dishonest performance of regulated activities, that clients should have the right to have their complaints determined by the Financial Ombudsman and any eligible claims not met by the adviser or its insurer should pass to the Financial Services Complaints Scheme, irrespective of the charging model.

Q13: What do you think are the main causes of unsuitable financial advice e.g. weak competition, complex products, etc?

There are two immediate causes of unsuitable advice: (i) lack of adviser capability and (ii) bad faith. There is also suboptimal advice, as mentioned below Q10, the immediate cause of which is either (i) lack of adviser capability or (iii) perverse incentives.

The underlying cause of all three is regulatory failure. It is the job of the FCA to help create a fair and transparent market that consumers can have trust and confidence in; and that requires setting up the incentives that operate in the marketplace, and to police it, in a way that incentivises good customer outcomes and deters bad ones.

A full analysis of where we believe the FCA is falling short and how it might be fixed is, as mentioned in response to Q1, better left for a Royal or Truth and Reconciliation Commission than dealt with here. However our responses to the regulators' consultation on Complaints Against the Regulators and to the Work and Pensions Committee's consultation on Protecting Pension Savers both contain many relevant suggestions.

Q14: How can we target and prevent unsuitable advice without imposing additional requirements on firms which provide suitable advice?

We are concerned that the Senior Managers and Certification Regime is not working as politicians intended. Too few managers are facing sanction. There may be merit in relaunching it as part of a wider initiative to introduce a fiduciary duty of care of firms toward their clients. One way to do this would be to borrow from the example of the banks, which take personal guarantees from company directors. Require senior managers to provide personal guarantees ensuring that they're first in the queue to meet any liabilities created by their wrongdoing and ensure that the security is called upon to the full in a few early, high-profile cases and you'll find standards transformed overnight.

Once this is done, professional indemnity fees and the FSCS levy (which some in the industry refer to as the regulatory failure tax) will both plummet, opening up the possibility of providing much enhanced protections for consumers without imposing unsustainable costs on honest and competent players in the industry (see later questions for details).

Q15: What role do you think there is for direct sales in a well-functioning consumer investment market?

In a well- functioning consumer market the optimum model is the one that delivers the most suitable outcome for the consumer at the best price, the best consumer protection and with the least consumer complaints.

The direct sales channel is a sales channel devoid of the need for the salesperson to find the best product on the market to suit the client, merely find the best that is on offer from within his own organisation. So not necessarily the best result and not necessarily any cheaper than obtaining a superior product through the medium of an IFA.

Direct Purchase is another option that cuts out all intermediation, as the customer purchases directly from the provider's website. This could be the optimum model, provided the customer is knowledgeable about the market, the products, the comparative costs and benefits and is willing to make the purchase knowing there is no investor protection available should he/she make an incorrect choice.

Furthermore, some investors believe that adviser distributed funds are the same as directly distributed funds, but with NAV clipped. Advisers feel they must masquerade as investment managers to compensate, but fail to beat low cost indexed funds. When markets are commoditised participants add service to compensate.

Q16: What protections are necessary for consumers buying direct?

There is a great need for clear and transparent explanation of products, terms, realistic returns, and costs. There are accessible well diversified low-cost funds from a number of providers. DIY Platforms often hide these options in favour of their top pick funds and own inhouse solutions.

We have already outlined (Q2/Q3) measures we believe could be taken before people open accounts with such platforms and before they conduct material transactions thereon, which together would represent steps in the journey toward achieving a high level of financial literacy.

To name just one example, until the FCA requires the investment management industry to fix the obvious liquidity mismatch involved in holding illiquid assets such as property, private equity, micro-caps and some types of bond in open-ended products by requiring them to convert into investment trusts, it is vital that consumers understand, before investing in an open-ended product containing such assets, that there are circumstances under which they may have to wait months or even years to withdraw their money, and that investing instead in a closed-ended vehicle such as an investment trust avoids this problem.

There may also be a need to consider whether supervision of providers and protections for consumer assets are adequate when held within such platforms. To date, such company failures have resulted in the preservation of assets other than cash (albeit with significant periods of enforced illiquidity), and in most cases cash consumed in liquidation costs has been made good by the FSCS. But it is only a matter of time before a platform that engages in reckless activities such as stock lending, perhaps combined with fraud, fails in circumstances in which assets purportedly held for clients don't exist, have been loaned out to third parties that are in default or have disappeared.

Note that whilst it is not necessary to split holdings across multiple platforms to keep within the FSCS payout ceiling (splitting holdings across several fund managers on the same platform which most customers should do, will achieve the required result), they may not know to do this so as things stand, losses exceeding the FSCS limit may will go unremedied.

There is therefore a case for the Pension Protection Fund covering assets held in SIPPs, for example, as these tend to account for the larger holdings on the platforms and their owners are the least able to make good any sums lost[4], or for clients to be prompted or even obliged to split holdings across multiple platforms to keep below the FSCS payout ceiling.

Q17: What safeguarding requirements should apply to those who distribute products to consumers through online platforms?

[4] We recognise that a funding mechanism would need to be agreed, and that any costs would, either directly or indirectly, be picked up by consumers

It is unclear to us what the FCA means by ‘safeguarding.’ Does it mean ‘supervision’, or ‘fiduciary duties to clients’?

If it means the former, we have outlined under Q16 why there may be a need for enhanced supervision of such platforms, and perhaps for additional safeguards or guarantees for client assets.

If it means the latter, this raises the question of duty of care, which we choose to deal with under Q29, below.

As a basic requirement it is expected that the products made available in this way will be regulated and have data available through public media as to underlying assets, performances, charges etc similar to all other funds in the particular market sector.

Q18: Are there any products or investment decisions which bring greater or specific risks of harm when consumers buy them directly?

It could be argued that the risks are higher when buying a fraudulent, poorly managed, complex or highly risky product directly, on the basis that a consumer might know less and hence be less well equipped to spot the potential downsides than an adviser. There is also the risk that the DIY investor could buy a perfectly good product that turns out to be unsuitable for his/her needs, again through lack of knowledge or understanding.

Set against that, our aim (Q2/Q3) is to encourage the FCA to adopt a policy of nudges and mandatory checks to ensure that every consumer embarks on a journey of financial knowledge acquisition appropriate to the nature of the decisions he or she is likely to be taking, so if our proposals are adopted, consumers will always have sufficient knowledge. And purchasing direct eliminates the possibility that the adviser may not be acting in good faith - for instance, he or she may recommend the product because of an undisclosed commission/backhander in the case of frauds. Purchasing direct also leaves the consumer without the protection of the compensation scheme, as there is no party against which to claim a mis-sale or a fraudulent sale.

It should be said of course that not many IFAs act fraudulently, and it is hoped that with additional diligence on the part of the FCA such criminals will be removed from the marketplace.

Q19: How can we better ensure that those who have the financial resources to accept higher investment risk can do so if they choose, but in a way that ensures they understand the risk they are taking?

Accepting higher risk may have more to do with time horizon than wealth. The FCA seems to be confusing risk appetite with capacity for loss.

Furthermore, this question touches upon the thorny issue of the regulatory perimeter. As the FCA's current Chair and former Chief Executive have admitted to the Treasury Committee, even they would struggle to describe its current location.

We believe that the perimeter must be extended, and that it must be clearly signposted. Lending to SMEs (outside the scope of this exercise) and investment by consumers into illiquid investments (very much within) should be brought unambiguously inside the perimeter.

Taking this step would remove the need for a false dichotomy between high net worth, sophisticated and professional investors and everyone else. The distinction is pointless. Losing money to a high-risk or fraudulent investment can be just as catastrophic for the former category of consumers, who may allocate more capital to such schemes because they've got more to start with. Indeed it could be worse for them, because the asset-rich tend typically to be older, so they may be less well placed to rebuild their wealth.

The universe of high net worth individuals also includes a great many people who should not be regarded as sophisticated or professional investors; indeed, some may be vulnerable. These may include elderly people with dementia, individuals who have received financial settlements following accidents or medical negligence and those who have inherited sizable sums but had no previous experience of managing capital.

The approach we outline in our reply to Q2/Q3 of this document and which informs much of our approach is that there should be a much enhanced focus on ensuring that consumers acquire more knowledge and confidence as they are faced with, or choose to engage with, increasingly complex investment options. So it seems logical to us that the option of investing in the most complex products should be limited to those who have acquired the greatest expertise, rather than those currently in possession of the most money.

One member of the team that worked on this document invests in deal-by-deal private equity and has done some angel investing. It happens that he has worked in a related field, so would currently qualify as a sophisticated or professional investor and not just by dint of the quantum of his investable assets. Had he not done so, it might be appropriate to ask him to complete an online course and test to demonstrate that he understands the sector. And it is vital that any firms marketing such investment opportunities to him understand that doing so is, in future, unambiguously a regulated activity.

One risk that comes with accepting the principle that there should be a class of higher-risk investment products, such as the (misnamed, since aspects of their promotion and operation are regulated) Unregulated Collective Investment Schemes, is that the regulator may use their status as grounds for supervising them and the firms that promote and operate them less proactively, if at all. An advantage to ending the distinction is that it would remove this risk.

Q20: How can we and the industry help consumers understand the benefits of diversifying their investments?

We would expect any online course provided to someone before they could gain access to an online platform providing LISA, ISA, SIPP and share dealing accounts to provide clear information on this topic, and to test that the consumer understands it.. For those consumers who would prefer to be advised the FCA should indicate where the consumer can find an appropriate adviser, who will explain the merits of diversification.

Q21: Would more investments benefit from 'prospectus-like' disclosure, and/or the disciplines involved in this? If so, in what circumstances?

Yes. We believe that all investments offered to consumers should come with this level of disclosure, and that there should be an unambiguous duty of care of firms toward consumers should a prospectus turn out to be inaccurate and consumers lose money as a result. We also believe that there should be an equally rigorous duty of care on the FCA requiring it to act when prospectuses or promotions are inaccurate or when financial promotions are issued that have not been approved by authorised firms.

Currently we operate in an environment in which having an authorised firm approve a promotion and ensuring that the promotion is accurate are largely optional activities, in that while breach of either is a criminal offence, prosecutions are almost unheard of, as are removals of firms and individuals from the register or the imposition of restitution orders. We believe that this is one of the FCA's most serious defects, and it has to change.

We cover the issue of financial promotions, including the need for prospectus-like filings, in our response to the Treasury's consultation on Financial Promotions.

We will provide proposals relating to a duty of care under Q29, below.

Q22: Should more investments be subject to continuing disclosure requirements after they are issued, and what liabilities should be attached to these disclosures?

Yes. Every prospectus should specify a frequency for routine reporting to clients and criteria for enhanced consultation and reporting, for instance when proposing a change to the investment criteria or manager, an intent to vary liquidity or leverage limits or otherwise to make material changes compared with the product that the prospectus led investors to believe they were subscribing to.

The same liabilities should be associated with failure to disclose changes as to issuing a misleading prospectus or promotion. The more products drawn into routine reporting the less there would be available for 'once off' instances of advice.

Q23: What do you think about how the current high net worth and self-certified sophisticated investor exemptions are working in practice and the level they are set at?

We argue (Q19, above) for the abolition of the HNW investor class and its replacement with a requirement to gain and/or demonstrate capability to understand complex products before a consumer can invest in them.

Q24: Firms: Have you relied on the exemptions recently to communicate promotions? Why did you do so? Consumers: Have you categorised yourself recently as high net worth or sophisticated? Why did you do so and what was your experience?

Our membership consists of over 2,700 people, a mix of industry figures and consumers. We are therefore unable to provide a consolidated answer to this question, as experiences are necessarily diverse.

Q25: What more can we do to help consumers understand the high net worth and sophisticated investor exemptions and what they mean for them in practice?

Nothing; we believe they are poor proxies for level of financial understanding, so should be abolished.

Q26: How can we make it easier for people to understand the risks of investment and the level of regulatory protection afforded to them when they invest?

Helping consumers understand the level of risk can be done in three ways:

- A traffic light-type product categorisation (Q5)
- Bringing all financial investments offered to consumers unambiguously within the regulatory perimeter
- Financial promotions, backed up by a prospectus, to which a robust duty of care applies - of the firm, and of the regulator

The traffic light system could incorporate logos for the FCA, FOS and FSCS, stating that the product is covered and what the limits are. All will be treated the same, because there will be no such thing as an unregulated collective investment offered to consumers in the environment we are proposing.

There is, of course, a risk that scammers will affix these logos to fake products. However, if the duty of care on the FCA to protect consumers operates as it should, the controlling minds of such boiler room frauds will be prosecuted and the results widely publicised, creating a powerful deterrent and ensuring that such instances quickly become very rare.

For consumers to achieve a good level of understanding of the risks attached to investments, greater capability, consistency and integrity is required of the FCA than has been the case recently, because a shortfall of these qualities allows too many cases to arise that cause rational consumers to fear entrusting capital to the sector.

With London Capital and Finance, for example, after the alleged fraud came to light, the FCA retrospectively deemed the product to be a mini-bond, something not defined in law or regulation at that time and thus claimed it was unregulated, perhaps to excuse its decision not to intervene after whistleblower Neil Liversidge tipped it off that the scheme was an alleged fraud. The consequence is that the FSCS sought to deny compensation to most of the victims. This behaviour has understandably lowered levels of confidence in all forms of investment products among consumers, who recognise that the regulator cannot be trusted to protect them and, worse, can retrospectively attempt to move the goalposts to deny them redress if things go wrong.

In addition the consumer should become familiar with his /her own risk profile, best conducted with a psychometric test. He/she should also become familiar with the mechanism for calculating his/her capacity for loss, as distinct to his/her willingness to accept investment risk.

Q27: What can be done to help consumers to better understand the circumstances in which they will be able to claim on the FSCS?

See our response to Q26, above.

Also, by requiring the issuers of investment products to make clear in their product literature which acquisition channels provide the protection of the FSCS and which don't.

Q28: What more can we do to ensure that when people lose money because of an act or omission of a regulated firm, they are appropriately compensated?

It may be that the financial ceiling for claims to be considered by the Financial Ombudsman needs to be significantly higher than the current £350,000, to reflect the sums of money commonly held in platforms. Alternatively, Tribunals may be a better option for larger claims[5].

It seems illogical and unjust that the upper limit to individual payouts by the Financial Services Compensation Scheme does not match that of the FOS, creating the problem that the FOS may issue a decision that pushes a firm into default but the FSCS is then unable fully to meet the claim.

There is also a longstanding problem, which emerged following attempts by the FSA/FCA and FOS to scapegoat IFAs for the collapse of The Connaught Income Fund Series 1, that the FOS and FSCS reach determinations on different grounds, so can come to different conclusions about the same case. In Connaught, the FOS found against a number of IFAs on the basis that it was 'fair and reasonable' that they should compensate victims; many went into default, so cases went to the FSCS. It is required to establish whether there is a chain of causation that would stand up in civil proceedings; on that basis it decided that the IFAs were not the cause of client losses, so refused to stand in the IFAs' shoes and honour compensation decisions issued by the FOS.

Finally, there is the topic of professional indemnity insurance. Currently, it operates on a 'claims made' basis, which means that it is the insurer in place on the date that a claim is made, not when the alleged error, omission or misconduct took place, that is liable for a claim. The problem with this approach is that most insurers are better at identifying risk than their clients and the regulator, so by the time claims start rolling in from consumers, the insurance industry has already in the main excluded them.

The FCA should require the industry to switch to a 'claims occurring' basis for its insurance provisions; it should also end the practice of allowing some larger firms to 'self insure'. This is another example of regulatory laxity that emerged in the Connaught case: Capita plc had self-insured its financial services arm, including Connaught's Operator, Capita Financial Managers Limited. Once the FCA accepted that the firm had issued misleading promotions and failed to communicate appropriately with customers and the regulator, Capita plc was in breach of its banking covenants and had to execute a fire sale of assets, its financial services arm included, to raise the cash to provide partial redress to the victims. Had it been insured by a third party the resultant delay, and the FCA's decision to accept only partial compensation, could have been avoided.

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[5] A move that has long been requested for dealing with disputes between SMEs and banks. A great advantage to the Tribunal system is that court-type standards of conduct are required of claimants and respondents: withholding or fabricating evidence or misleading the hearing can result in prosecution. Another is that both sides get to see and critically examine the other's position and evidence; under the Ombudsman system, the respondent gets to see and challenge the complainant's submission, but the opposite is not the case.

Q29: What more can we do to ensure that compensation is paid for fairly by those that cause the loss?

The text preceding this question frames it as being one concerned principally with the advice sector, but we have chosen to answer it in relation to the industry as a whole, as we see no reason for differential treatment.

The principal means by which we can ensure that regulated advisers are civilly liable for consumer losses that they cause is to introduce a fiduciary duty of care of advisers toward clients. Rather than discuss this in depth here, we refer you to three of our previous submissions to consultation exercises: Duty of Care, Complaints Against the Regulators and our response to the Work and Pensions Select Committee's Inquiry on Pension Scams.

It is important to stress that we believe this duty of care should extend to the FCA, in respect of consumers. If firms and individuals are in breach of regulations, taking action against them cannot be optional, as appears to be the case at present. The second and third of the above mentioned documents address this issue directly.

This raises the sensitive issue of civil liability of the FCA for losses suffered by consumers as a result of regulatory failure. Rightly or wrongly, parliament granted the FCA immunity from civil liability, excepting in cases relating to human rights breaches and bad faith (misfeasance/nonfeasance in public office) when it created the organisation by passing the Financial Services Act 2012. However, politicians intended that consumers should be able to receive redress from the FCA in cases where they suffered losses as a result of regulatory failure, and they required the FCA to establish a complaints scheme and independent investigator to achieve this goal.

Unfortunately over the years the FCA has parlayed that scheme into one that makes it almost impossible for the public to obtain such compensation, a situation that provoked the outgoing Complaints Commissioner, Antony Townsend, to call for a public consultation. Worse, the FCA decided to use that consultation as an opportunity to further limit the potential for such redress to be paid.

Our response to that consultation makes a robust case for the regulators working with genuine consumer advocates to specify a fit-for-purpose complaints scheme that fulfils the obligations placed on it by the 2012 Act. If the FCA does not agree to this we believe that politicians should remove the FCA's exemption from civil liability.

The irony is of course that should the FCA be required to compensate victims of its mis-regulation it will simply pass the costs on to the regulated community, and thus on to the clients of the regulated community in due course. Where is the punishment for the individuals within the FCA that may have been responsible for its sub-optimal performance as a regulator?

Whatever happens to the complaints scheme, there is a need to deal fairly with legacy cases. We propose (Q1, above) that a Commission, somewhere between the Royal one into financial services that took place in Australia and truth and reconciliation ones that have dealt with longstanding injustices in South Africa and elsewhere should be introduced to deal with historic cases in UK financial services. The focus should be on getting firms and the regulator to admit to past failings, compensate the victims and have the guilty parties agree to leave the industry, with prosecution and removal of permissions as the penalties for failing to engage cooperatively with the process.

Q30: What do you think should be done to help ensure that the 'polluter pays' for unsuitable advice?

Q31: What do you consider to be the right balance of approaches to ensure we provide an appropriate level of protection to consumers?

We find it telling that this 'polluter pays' section refers only to the advice sector (typically, 'the little guys'); when it comes to larger firms, the expectation in the FCA's consultation document seems to be that the polluter probably won't pay, that the costs of failure and misconduct will be socialised. Our response therefore ignores the FCA's presumption and is instead sector-agnostic.

We agree that the polluter should pay, wherever possible. However, it is intrinsic to the nature of the advice and consumer investment markets that the amounts of capital affected are many times larger than the fees extracted. Unless all firms are required to maintain non-viable large balance sheets - a stipulation that would reduce the number of market participants, and hence competition, and would also raise fees to unsustainable levels - when things go wrong, whether through negligence or dishonesty, the firm concerned is unlikely to have sufficient resources to repay the debt in full.

The principal solution to this conundrum is to reform the professional indemnity market so all consumer claims are covered and premiums more accurately reflect each individual adviser's risk profile, rather than forcing consumers to bear the negative externalities or socialising them within the industry's honest and capable majority.

We therefore endorse the principle that professional indemnity premiums should be more accurately risk-based, where risks include those created by type of activity undertaken and the track record of the individual adviser.

A potential downside to this approach is that an adviser could buy cheap insurance on the basis that he tells the insurer he will avoid claim-generating activities such as defined benefit pension transfers and the sale of complex products and claim-generating personnel such as ARs, then pivots into the high-risk activities. The solution, which should be considered as part of a process led by the FCA of rebuilding the PI market as described under Q28, above, is that advisers should be authorised to conduct very specific activities. Insurers would then be able to price policies based on advisers' register entries, knowing that departure from the permitted constraints would constitute a regulatory breach that would - hopefully - be noticed by Supervision and reversed, with appropriate sanction following under the SMCR.

The above presupposes higher levels of proactivity from the FCA than it typically displays, but we submit that our expectations are reasonable and it is for the FCA to close any capability gap.

Another advantage to risk-based professional indemnity pricing is that insurers will do due diligence into each adviser's background, qualifications, experience and claims history and experience.. There are individuals who have been associated with numerous past examples of poor advice and scams who have habits of turning up at one firm after another. If their presence on a company payroll rendered them uninsurable, the bad apples would be removed from the industry.

Whether an adviser's conduct costs are met in part or in whole by the insurer, the FSCS, consumers or, where there has also been regulatory failure, the FCA, it is the case that the polluter has not paid the full cost. This being so, it is important that there are other ways in which the negative externalities are faced by the individuals

Given that it is not firms that cause loss to consumers, it is individuals who cause the loss. Every claim made to the FSCS will have the name of the adviser on it. Hence our recommendation that it is individual registered advisers required to hold personal PII cover, which would become the first port of call in the event of a valid claim for compensation. Each registered individual in the marketplace should have their own PII with premiums based on their qualifications, their product range, their product volume and their claims history, Any claim not met in full (including costs) should require immediate de-registration and removal from the marketplace until the debt is cleared. This would render 'phoenixing' firms irrelevant

In the consultations mentioned under Q29, above, we express concerns at the FCA's reluctance to use the full range of tools currently given to it by parliament. Prosecutions, bans and fines are far too seldom witnessed. For economic incentives to be aligned in a way that gives a reasonable prospect for customer treatment to be improved, this must change. We question whether this is achievable since it seems to have at its root longstanding problems with culture, incentives, governance and organisational memory.

Q32: Do you have any views on how the AR regime is working in practice?

We have expressed some reservations about this, and proposed a market-based remedy, in our reply to Q30/Q31, above.

Q33: How can people be better protected from scams?

Q34: What do you think are the most suitable and proportionate remedies to further tackle scams and other online investment harms?

We address these questions in detail in our response to the Work and Pensions Committee consultation on Pension Scams, and in additional papers submitted in response to requests from that Committee on a Proposal for a Financial Services Joint Taskforce. Our responses to the Treasury consultation on financial promotions and to the regulators' one on their complaints scheme are also highly relevant.

However, the changes we propose to the legislation and to the operations of the FCA and other statutory bodies in the above documents are not in themselves sufficient to tackle the scam pandemic, nor will they rebuild the level of confidence among consumers necessary to encourage those who currently don't take advantage of simple investment options to do so.

For these things to happen, the regulator must be many times more agile, proactive, transparent and accountable to elected politicians and genuine consumer representatives than is currently the case. We are agnostic as to whether the solution is a radically revised FCA, or a new, replacement organisation.

Q35: What opportunities do you think can emerge for the consumer investment market from innovation?

In the UK, virtually all financial advisers are adviser-distributors. The conduct risk is almost wholly attributable to poor policing of the advisers on the distribution side. If advice and distribution were to be separated, as is the case in other markets including India and Australia. The FCA could then focus resources on where the risk lies, the distributors.

With the removal of incentives to misbehave on the advice side, conduct risk is mitigated. Capability can be managed by professional bodies.

Effectively, the adviser becomes the consumer's own personal regulator and can help protect consumers from bad actors.

Also the generic advice and financial education nature of the non-intermediating financial planning, means that this service can be delivered to groups at a fraction of the cost and well within levels that consumers are willing to pay. This remedy plugs the advice gap, and eases the burden on the FCA.

Q36: What do you think are the main risks of innovation for consumers?

Lowering the cost to a firm of obtaining regulatory approvals, provided it does not entail lowering standards, can be a public good, because it enables new firms to enter the market, potentially (though not necessarily) with new and different products. Enabling a firm to achieve approvals faster, again provided there are no shortcuts, may be of marginal benefit to consumers if the firm is offering new products or will increase competition because those enhancements will be experienced a little sooner.

The risk is that poorly capitalised firms will sail through streamlined regulatory processes and offer poor quality and even fraudulent products to the marketplace. Lendy and other peer-to-peer platforms are ignoble testaments to the FCA's at best mixed track record in policing the regulatory sandbox - especially given that non-fraudulent firms that have not caused consumer detriment such as Bond Mason were held back.

The image of a fleet of foot regulator that creates an accelerated permissions regime for innovative firms is one we would all like to buy into, but our observation is that it is unwise to attempt to run before one can walk, and the FCA has a long way to go before it can enjoy sufficient confidence from us and other campaigning groups in its day-to-day operations for us to feel comfortable about it promoting innovative shortcuts.

Q37: What are the barriers to innovation and effective competition in this market?

We believe there is a high regulatory burden in the market and feel that the adoption of a legally enforceable fiduciary duty as described earlier would create a far more efficient market that could operate in a more agile and efficient manner.

Q38: What more can we do to facilitate effective competition and encourage firms to develop innovative products and services which help consumers to invest?

For start-ups there can also be the Catch-22 situation that investment is unlikely to be forthcoming unless regulatory approval is either granted or certain, while the cost of obtaining authorisation and relevant permissions may be high, especially for a firm that has no track record and no incumbent compliance team.

The FCA could usefully focus on ways of fixing that conundrum, rather than accelerating the process. For instance, it could grant conditional permissions[6] or could engage with prospective investors to help firms through the process without cutting corners. Controversially, the FCA could perhaps provide non-financial assistance such as advice to help firms reach the required standards and develop business models and products it would be comfortable to authorise.

[6] Contingent on an agreed balance sheet strength, hiring of certain key personnel or passing of agreed milestones

Q39: Have there been initiatives to promote innovation and competition in other countries that may be relevant for the UK?

Yes, India. Oct 2020. SEBI split Advice and Distribution. Distributors cannot call themselves financial advisers or financial planners. Distributors must call themselves Mutual Fund Distributors. Both roles are regulated. Advisers cannot receive fees from products, or levy ad valorem fees. They refer to D2C platforms. D2C Platforms have started to offer free advice to gain membership.

...and Australia. Fee-for-service banned. $5bn compensation paid to consumers. Now introduced yearly opt-in to ongoing service. More clarity now on advice and distribution, though didn't go as far as splitting vertically integrated firms, made it much more difficult to be one.

End.