

## Finalised guidance

# Retail Distribution Review: Independent and restricted advice

June 2012



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## 1 Introduction

- 1.1 The Retail Distribution Review (RDR) resulted in new and updated rules, which will improve the clarity with which firms describe their investment advice services to consumers. From the end of 2012, firms providing advice on retail investment products to retail clients will need to describe these services as either ‘independent’ or ‘restricted’. We have also updated the rules that set out what is expected of a firm that describes its advice as being independent.
- 1.2 The new standard for independent advice is intended to ensure that such advice is genuinely free from bias towards particular solutions or any restrictions that would limit the range of solutions that firms can recommend to their clients<sup>1</sup>. In providing independent advice, a firm should not be restricted by product provider, and should also be able to objectively consider all types of retail investment products which are capable of meeting the investment needs and objectives of a retail client.
- 1.3 Restricted advice, which is advice that does not meet the standard for independent advice, will come in many different forms. While a firm needs to describe the nature of its restricted advice service to clients, it is free to choose the words that are appropriate for its service.
- 1.4 Since the RDR independent and restricted advice rules were published, we have received a number of questions from firms. This guidance addresses the common points being raised, with the aim of helping firms to implement the new requirements. As most questions raised have been around the standard for independent advice, this is the focus of this guidance.
- 1.5 This paper is structured as follows:
- Section 2 outlines the key components of the standard for independent advice;
  - Section 3 covers the requirements for firms providing restricted advice;
  - Section 4 discusses the requirements for how firms hold themselves out;
  - Section 5 discusses a number of advice tools and investment strategies, and how their use may influence the ability of firms to meet the independent advice rules; and
  - Section 6 is on professional standards and how differences between the qualifications and skills of advisers may affect the ability of advice to meet the independent advice rules.
- 1.6 Unless indicated otherwise, the rules referred to in this paper are those that come into force on 31 December 2012. This paper does not contain all of the rules and guidance in the Handbook relevant for

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<sup>1</sup> Unless otherwise indicated, ‘client’ is used in this document to mean ‘retail client’.

independent and restricted advice. For all of the relevant rules and guidance, firms should refer to the Handbook.

## 2 The standard for independent advice

- 2.1 ‘Independent advice’ is defined in the Handbook as *‘a personal recommendation to a retail client in relation to a retail investment product where the personal recommendation provided meets the requirements of the rule on independent advice (COBS 6.2A.3R)’*.
- 2.2 The requirements of the rule on independent advice (‘the standard for independent advice’) are that the personal recommendation<sup>2</sup> is:
- (a) based on a comprehensive and fair analysis of the relevant market; and
  - (b) unbiased and unrestricted.

### Retail investment product

- 2.3 ‘Retail investment product’ is defined in the Handbook as:
- (a) *a life policy; or*
  - (b) *a unit; or*
  - (c) *a stakeholder pension scheme; or*
  - (d) *a personal pension scheme; or*
  - (e) *an interest in an investment trust savings scheme; or*
  - (f) *a security in an investment trust; or*
  - (g) *any other designated investment which offers exposure to underlying financial assets, in a packaged form which modifies that exposure when compared with a direct holding in a financial asset; or*
  - (h) *a structured capital-at-risk product;*
- whether or not any of a) to h) are held within an ISA or a child trust fund (CTF).*

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<sup>2</sup> See the Perimeter Guidance Manual for further guidance on when advice on investments is regulated by the FSA, in particular 8.24 to 8.30 and 13.3 Q19-Q20.

- 2.4 A personal recommendation in relation to any of the products in this list must meet the standard for independent advice to be described as such.
- 2.5 The definition of retail investment product is intentionally broad to ensure that all comparable investment products sold to retail clients on an advised basis, including those developed in the future, are subject to the same relevant selling standards, for example the requirement to be remunerated by adviser charges. To determine whether a product is captured by the definition of ‘retail investment product’, the characteristics of that particular product would need to be considered. In general, we expect there to be very few types of investment products sold to retail clients that would not fall within the definition. Examples of financial instruments that are not retail investment products would include a share in an individual company whose primary business is not investing in two or more financial assets<sup>3</sup>, an individual fixed interest security and an individual derivative, where the exposure to the relevant asset is not modified in any way.

#### Relevant market

- 2.6 COBS 6.2A.11G says that a relevant market should ‘*comprise all retail investment products which are capable of meeting the investment needs and objectives of a retail client*’. For example, if a client indicates that they are only interested in ethical and socially responsible investments, it is clear that there is a range of products that would never be suitable for them, namely non-ethical investments. Their relevant market would exclude non-ethical investments, and an adviser would not need to consider these products when forming independent advice for such a client. So, a relevant market in the context of the standard for independent advice is defined by a client’s investment needs and objectives and not, for example, by product or service types.
- 2.7 ‘Investment needs and objectives’ need to be assessed on an individual client basis, so we do not believe it possible that many firms can say unequivocally upfront what products may be capable of meeting the investment needs and objectives of their clients. We expect, therefore, that the majority of firms providing independent advice will need to be able to provide advice on all types of retail investment products. A firm could decide that it will specialise in certain financial situations, for example saving for retirement, but that does not necessarily mean that it can rule out in advance advising on certain retail investment products if it provides independent advice.
- 2.8 However, if a firm can identify a common relevant market across all of its clients that does not include certain retail investment products, it would not need to consider such products when giving independent advice. To not consider certain retail investment products, the firm would need to be able to market itself in a way that attracted only the intended type of clients, and only take on the intended type of clients. This would mean that both the firm and consumers would need to be able to easily identify whether the consumers’ relevant market matched the firm’s specialism, for the firm to provide independent advice.

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<sup>3</sup> Shares in investment trusts and open-ended investment companies are captured by the retail investment product definition.

- 2.9 If a firm chooses to specialise in a particular relevant market, *‘it should not hold itself out as acting independently in a broader sense. For example, a firm “Greenfield”, which specialises in ethical and socially responsible investment, should not hold itself out as “Greenfield Independent Financial Advisers”.* *“Greenfield – providing independent advice on ethical products” may be acceptable’* (COBS 6.2A.4G(2)).
- 2.10 In terms of disclosure, *‘if a firm provides independent advice in respect of a relevant market that does not include all retail investment products, a firm must include in the disclosure an explanation of that market, including the types of retail investment products which constitute that market’* (COBS 6.2A.6R(2)).
- 2.11 We would expect a firm not to rely solely on disclosure to ensure it only takes on clients whose relevant market matches the firm’s specialism. For example, a firm should ask initial questions of prospective clients to determine whether their investment objectives and needs align with that of its target market.
- 2.12 In the rules, we use an example of ethical and socially responsible investments as a market that a firm could specialise in and hold itself out as independent because it appears to meet the tests described above, i.e.:
- if clients indicate that they are only interested in ethical and socially responsible investments, then a firm would not need to consider investments that do not meet this criteria, and can therefore narrow the range of products that it gives advice on;
  - clients should be able to easily identify a preference for ethical or socially responsible investments, and so be able to self-select with a high degree of accuracy;
  - a firm should be able to market itself in a way that only attracts clients with a preference for ethical and socially responsible investments; and
  - a firm should be able to easily confirm whether its service is appropriate for each new client, i.e. that it can consider all of the products within each client’s relevant market.
- 2.13 We expect there to be a limited number of common relevant markets in which a firm could specialise, restrict its product range accordingly and meet the independent advice rules. We have set out below three further examples; a firm may be able to provide independent advice to:
- clients who want Islamic financial investments, and never advise on non-Islamic financial investments;
  - trusts and charities, and never advise on pensions; or
  - clients who want to take an income from their pension, and provide advice only on annuities and drawdown products.

**‘Comprehensive and fair analysis’, ‘unbiased and unrestricted’**

- 2.14 This section sets out some of our expectations on meeting the standard for independent advice, in particular the twin tests of being ‘based on a comprehensive and fair analysis of the relevant market’ and ‘unbiased and unrestricted’, whether or not a firm is specialising in a relevant market.

*Excluding product types from consideration*

- 2.15 If a firm cannot or will not advise on a particular type of retail investment product, and that product could potentially meet the investment needs and objectives of its new and existing clients, then its advice will not meet the standard for independent advice. In other words, the justification for a firm excluding types of retail investment products from its range needs to be centred on the client. As an example, the fact that a firm’s professional indemnity insurance policy specifically excludes certain products would not be a valid reason for never advising on such products.
- 2.16 However, we do not expect a firm to actually recommend all products captured by the broad definition of retail investment product as a matter of course. It may be possible for a firm to conclude for many clients, early on in the advice process, that certain product types are not going to be suitable, and therefore not consider these product types further for those clients.
- 2.17 We propose to consult on new rules for unregulated collective investment schemes (UCIS) during 2012; this will make clear our expectation that UCIS will be suitable for very few retail clients, if any. Our current requirements already limit the categories of investors to whom UCIS can be marketed (see COBS 4.12). A firm’s independent status will not be affected if it never recommends these products because it deems them to be unsuitable for its clients.
- 2.18 Where we have identified high-risk products and recommended that they should not reach retail investors in the UK, a firm would not need to consider them for its clients to meet the standard for independent advice.<sup>4</sup>

*Reviewing product markets*

- 2.19 A firm that provides independent advice should base their recommendations on a comprehensive and fair analysis of the relevant product markets, which will include products, such as collective investment schemes, that are manufactured outside the UK but are widely available to UK consumers.
- 2.20 As the standard for independent advice applies to the personal recommendation of a particular retail investment product (such as units in a collective investment scheme), we expect firms to consider the product market at this level (so, for example, a firm should not restrict its advice to certain collective investment schemes, and should base the selection of units in a collective investment scheme for a client on the basis of a comprehensive and fair analysis of the market for this product). We make this expectation clear in the Handbook through the following guidance: ‘*A personal recommendation on a retail investment product that invests in a number of underlying investments would not of itself meet*

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<sup>4</sup> For example, see GC11/28: Traded Life Policy Investments, November 2011.

*the requirements for providing unbiased and unrestricted advice even if the retail investment product invests in a wide range of underlying investments’ (COBS 6.2A.14G).*

- 2.21 A client may instruct a firm to limit the scope of its advice, for example to only give personal recommendations relating to an identified portion of their assets or in relation to the desirability of investing in a specific investment. In such circumstances, a firm that provides independent advice would only need to consider the retail investment products capable of meeting the client’s stated investment needs and objectives. The range of retail investment products that should be considered will depend on the nature of the client’s request.
- 2.22 There is guidance in the Handbook on the degree to which firms should look beyond retail investment products when providing independent advice: *‘In providing unrestricted advice a firm should consider relevant financial products other than retail investment products which are capable of meeting the investment needs and objectives of a retail client, examples of which could include national savings and investments products and cash deposit ISAs’ (COBS 6.2A.17G).*

#### *Product provider influence*

- 2.23 We have been asked how certain product providers’ business models or distribution strategies may have an impact on a firm’s ability to provide independent advice.
- 2.24 If an independent advisory firm cannot access products from a particular provider, for reasons linked to the provider’s business model, its advice may still meet the standard for independent advice. For example, it may be that the advisory firm has access to a comprehensive range of comparable products, or that it provides advice on products that it cannot access, but does not execute the recommendations itself.
- 2.25 Conversely, to satisfy the standard for independent advice, *‘a firm should ensure that it is not bound by any form of agreement with a retail investment product provider that restricts the personal recommendation the firm can provide or imposes any obligation that may limit the firm’s ability to provide a personal recommendation which is unbiased and unrestricted’ (COBS 6.2A.15G).*

### **3 Restricted advice**

- 3.1 ‘Restricted advice’ is defined in the Handbook glossary as:
- (a) *a personal recommendation to a retail client in relation to a retail investment product which is not independent advice; or*

(b) *basic advice*.<sup>5</sup>

- 3.2 In other words, if a personal recommendation on a retail investment product does not meet the standard for independent advice, then it is restricted advice.
- 3.3 Restricted advice must meet the same suitability, inducement<sup>6</sup>, adviser charging and professionalism standards as independent advice. The key difference in our requirements is in disclosure. In its written disclosure, a firm that provides restricted advice must explain the nature of the restriction (COBS 6.2A.6R). A firm must also provide oral disclosure if it engages in spoken interaction with a retail client (COBS 6.2A.9R).
- 3.4 The rules allow firms flexibility in how they describe their restricted advice services, so long as they are being fair, clear and not misleading in their communications. A firm can, for example, explain that it reviews the whole market for the particular products on which it gives advice, if this is an accurate description of its service. A firm should not, however, give the impression that it has restricted its product range to those products that are most suitable for a particular client.
- 3.5 Establishing that a recommendation of an investment product is suitable will normally require consideration of a client's existing investments, regardless of whether independent or restricted advice is being provided. The way in which a firm discloses its restricted advice service should not be a barrier to the firm doing this. For example, the disclosure may use the words 'we only offer products from certain product providers', and this should not have an impact on the ability of the firm to consider whether the client's existing investments would affect the suitability of the new recommendation. If a firm can only recommend certain products, then we would not expect to see it giving advice to clients to transfer their investments to its restricted product set unless this was in the best interests of the client.
- 3.6 'Simplified advice' is not a defined term in the Handbook, but has been adopted to describe streamlined advice processes, typically automated, which aim to address straightforward needs of consumers. Simplified advice is a form of restricted advice because it does not consider all types of retail investment products that may be suitable for consumers. Therefore, any firm that provides simplified advice should not hold itself out as acting independently for its business as a whole, and must comply with the disclosure rules for restricted advice.

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<sup>5</sup> COBS 9.6 sets out rules for giving basic advice on a stakeholder product. Basic advice is a short, simple form of financial advice which uses pre-scripted questions to determine whether a stakeholder product within a firm's range will be suitable for a customer.

<sup>6</sup> The rule on inducements (COBS 2.3.1R) bans the payment of a fee or commission, or the provision of the non-monetary benefit, unless certain conditions are met, namely that it does not impair compliance with the firm's duty to act in the best interests of the client, is clearly disclosed to the client before the provision of the service, and is designed to enhance the quality of the service to the client.

## 4 Communicating the nature of a firm's advice services

- 4.1 The Handbook contains requirements for a firm holding itself out as providing independent advice, which are covered in this section. Firms should refer to COBS 6.2A.5R to 6.2A.9R for the requirements specific to disclosure.
- 4.2 The rule for a firm holding itself out as providing independent advice is (COBS 6.2A.3R):
- (1) *A firm must not hold itself out to a retail client as acting independently unless the only personal recommendations in relation to retail investment products it offers to that retail client are:*
- (a) *based on a comprehensive and fair analysis of the relevant market; and*
- (b) *unbiased and unrestricted.*
- (2) *Paragraph (1) does not apply to group personal pension schemes if a firm discloses information to a client in accordance with the rule on group personal pension schemes (COBS 6.3.21R).*
- 4.3 A firm will 'hold itself out' through a variety of means, some of which are untargeted, an obvious example being a firm's trading name. If a firm includes 'independent' in its trading name, it is likely to be holding itself out as providing independent advice to all clients that approach the firm. All personal recommendations on retail investment products provided by such a firm should therefore meet the standard for independent advice.<sup>7</sup> This expectation is made clear in COBS 6.2A.4G(1), which says that 'a firm that provides both independent advice and restricted advice should not hold itself out as acting independently for its business as a whole'.
- 4.4 If a firm provides both independent advice and restricted advice on retail investment products, there are a number of ways in which it could make it clear to clients that it offers both. For example, a firm may have a name that does not include 'independent' and offer clients who approach it a choice of independent or restricted advice, or it may have two or more trading names to clearly separate its independent advice and restricted advice business arms.
- 4.5 Means of communicating the nature of a firm's advice services, other than the firm's name, will be both untargeted and available for anyone to see (for example, website text) and targeted to specific individuals (for example, an individual adviser's business cards handed out to a client in personal meetings). If a firm provides both independent advice and restricted advice, it should not hold itself out as independent to any client to whom it does not provide independent advice. We expect a firm to consider where and how it uses the term 'independent advice' to ensure that it is consistent with its obligation to be fair, clear and not misleading in its communications with clients. Essentially, the consumer should be left in no doubt of the type of advice they are receiving.

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<sup>7</sup> Such a firm, however, could also provide basic advice on stakeholder products, so long as the nature of the advice service being provided is clear to consumers. COBS 6.2A.4G(3) says that *a firm that provides basic advice on stakeholder products may still use the facilities and stationery it uses for other business in accordance with the rule on basic advice on stakeholder products: other issues (COBS 9.6.17R(2)).*

### Principal firms and appointed representatives

- 4.6 A directly authorised firm that has one or more appointed representatives (ARs) is responsible for ensuring that those ARs are meeting the relevant selling standards, including the independent advice rules. Such directly authorised firms are referred to as ‘principal firms’ in the remainder of this document.
- 4.7 An AR should not hold itself out as acting independently for its business as a whole unless all of its personal recommendations meet the standard for independent advice.
- 4.8 An AR might use its own branding or branding that is linked to its principal firm in some way. Even when using its own branding, GEN 4.3 requires an AR to refer to its principal firm in letters and electronic equivalents to retail clients that are sent with a view to, or in connection with, the AR carrying on a regulated activity. If a firm’s ARs provide a mix of independent and restricted advice, we would not expect the name of the principal firm to include ‘independent advice’, or similar, because of the potential to mislead the consumers of its ARs.

## 5 Advice tools and investment strategies

- 5.1 A firm may adopt a number of tools and strategies to help it advise clients and manage their investments. This section discusses a number of these and how their use may influence the ability of a firm to meet the standard for independent advice. Specifically, this section covers the use of panels, platforms, model portfolios and referrals to discretionary investment services.<sup>8</sup>
- 5.2 It is worthwhile reiterating that personal recommendations made through such means must be suitable and in the client’s best interests, **regardless** of whether the firm is providing independent or restricted advice. We have expressed concern about levels of suitability in a number of circumstances. For example, as we pointed out in recent guidance on suitability (FG 11/05<sup>9</sup>), we have seen evidence of firms failing to challenge cases where automatically generated investment selections (for example, from model portfolios or asset-allocation tools) are unsuitable for individual customers. The content in this section on suitability and client’s best interests is equally applicable to restricted advice.
- 5.3 A firm could choose to use a third party to conduct product research as part of the tools and strategies discussed in this section. For example, a firm could buy in product research to help construct its panel or model portfolio, or make use of asset allocation software tools. We include guidance in the Handbook on such situations:

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<sup>8</sup> For guidance on distributor-influenced funds see: FG 12/04: Distributor-influenced funds, February 2012.

<sup>9</sup> FG 11/05: Assessing Suitability: Establishing the risk a customer is willing and able to take and making a suitable investment selection, March 2011.

*If a firm chooses to use a third party to conduct a fair and comprehensive analysis of its relevant market, the firm is responsible for ensuring the criteria used by the third party are sufficient to meet the requirement. For example, criteria which selected retail investment product providers on the basis of payment of a fee (or facilitation of adviser charges), whilst excluding those not paying a fee (or such a facilitation) would not meet the comprehensive and fair analysis requirement (COBS 6.2A.20G).*

#### **Panels**

- 5.4 A firm can use research to distil the product market into a panel and then select a product from the panel when giving independent advice.

*A firm would need to ensure that any panel is sufficiently broad in its composition to enable the firm to make personal recommendations based on a comprehensive and fair analysis, is reviewed regularly, and that the use of the panel does not materially disadvantage any retail client (COBS 6.2A.18G).*

*When using a panel a firm may exclude a certain type or class of retail investment product from the panel if, after review, there is a valid reason consistent with the client's best interests rule, for doing so (COBS 6.2A.19G).*

For example, a firm may feel that certain products have a high level of risk that is not appropriate for its client base and so exclude them from its panel.

- 5.5 However, a firm that provides independent advice needs to be able to advise off-panel if that would be in the best interests of a particular client. To do this, its advisers should maintain an awareness of what is and is not included in the panel, so they can identify clients for whom an off-panel solution would be suitable. For example, if a client wants ethical investments and a firm does not have a product on its panel that is consistent with this preference, we would expect the firm to review the market for a suitable ethical product.

#### **Platforms**

- 5.6 A similar rationale applies to the use of platforms – as well as discount brokers and other channels for buying investments – as for panels. A firm can use platforms in providing independent advice, but need to remain aware of the limitations of its chosen platform and advise 'off-platform', or through another platform, where this is best for a client.
- 5.7 The current market is changing on a frequent basis and – generally – platforms do not offer products from the whole of the retail investment product market. So, in the current market, we expect it to be very rare, if possible at all, that a firm could use a single platform for all of the investment business of all of its clients and meet the standard for independent advice.
- 5.8 COBS 6.2A.4AR says that:

*In complying with COBS 6.2A.3R<sup>10</sup>, a firm which:*

- (a) holds itself out to a retail client as acting independently; and*
- (b) relies upon a single platform service to facilitate the majority of its personal recommendations in relation to retail investment products;*

*must take reasonable steps to ensure that, as appropriate, the platform service provider bases its selection of retail investment products on a comprehensive, fair and unbiased analysis of the relevant market.*

- 5.9 A recommendation to any client to use a particular platform-based service should be in that client's best interests. Examples of aspects that a firm should consider include a platform's charges and features, and the wrappers and/or products available on that platform. For further guidance on the use of platforms see the factsheet 'Using platform-based investments and the independence rule'.<sup>11</sup>

### Model portfolios

- 5.10 We use 'model portfolio' to mean a pre-constructed collection of designated investments, including some retail investment products, that meets a specific risk profile, sometimes offered with a periodic rebalancing of investments to maintain a consistent asset allocation. Model portfolios allow a firm to pre-determine what will generally be its advised asset allocation for certain investment objectives or attitudes to risk, and to distil its product research in line with these asset allocations.
- 5.11 Some individual retail investment products have similar characteristics to model portfolios, such as funds of funds, and a firm may use the term model portfolio, or similar, to describe them. The guidance elsewhere in this document is relevant to such products.
- 5.12 If a firm is constructing its own model portfolios, which include one or more retail investment products, for use in providing independent advice, it should ensure that it bases its selection of retail investment products on a comprehensive and fair analysis of relevant product markets. If a firm is using model portfolios constructed and managed by a third party, it should ensure the criteria used by the third party to select retail investment products are sufficient to allow the firm to meet the independent advice rules.
- 5.13 Before recommending a model portfolio, a firm should consider each product in the model portfolio within the context of the whole portfolio, in light of the client's individual circumstances. For example, a client may have preferences about the types of investments they wish to make, such as ethical or socially responsible investments, or have existing exposure to sectors or assets held within

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<sup>10</sup> COBS 6.2A.3R is the rule on firms holding themselves out as providing independent advice.

<sup>11</sup> This factsheet provides information on the use of platforms and the independent advice rules, and good and poor practice examples. Whilst this material relates to the current COBS rules, we state that it is also relevant to the independent advice rules introduced by the RDR.  
<http://www.fsa.gov.uk/smallfirms/resources/factsheets/pdfs/platforms.pdf>.

the model portfolio. The model portfolio as a whole, rather than the individual products held within it, should be considered when determining whether the model portfolio is suitable given the client's attitude to risk.

- 5.14 If any aspect of the model portfolio is not suitable or consistent with the client's investment needs and objectives, then either: 1) the model portfolio should not be recommended; or 2) the model portfolio should be tailored so that it is suitable (which would make it a 'bespoke portfolio'). In addition, the firm should consider whether use of the model portfolio as a whole is in its client's best interests, which will entail, among other things, ensuring that the model portfolio charges are appropriate for each individual client's circumstances.
- 5.15 In giving independent advice, a firm should not restrict its advice to certain model portfolios, or treat model portfolios as the default solution, regardless of whether these can be tailored for individual clients. Rather, it should be able to recommend other investment solutions and advise on retail investment products not held in the model portfolios, if these could meet the investment needs and objectives of its clients. Advisers should maintain a good understanding of the make-up of any model portfolios their firm uses, and the situations in which the model portfolios would – and would not – be a suitable recommendation.

### Discretionary investment services

- 5.16 This section discusses the obligations of a firm when recommending a discretionary investment service to a client, if it is holding itself out as providing independent advice.
- 5.17 A 'recommendation' in this context is used to mean a situation where an adviser has considered a client's personal circumstances and decided that a discretionary investment service is the right solution for them. In addition to recommending a discretionary investment service, the adviser may play a part in determining the discretionary mandate, or provide information to the discretionary investment manager (DIM) on the client's risk profile or investment objectives. The adviser may have an ongoing relationship with the client, in which the investments managed by the DIM are just part of the client's overall financial situation that the adviser considers in their periodic reviews.<sup>12</sup>
- 5.18 Such recommendations would normally not be considered 'personal recommendations', if they do not relate to one or more specific financial instruments. The standard for independent advice only applies to personal recommendations on retail investment products.
- 5.19 However, to meet its obligations under the Principles for Businesses<sup>13</sup> if a firm is providing independent advice, it should objectively consider a wide range of investment solutions in the market before recommending a client use a discretionary investment service. Recommending a discretionary

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<sup>12</sup> The DIM and adviser will need to ensure between themselves that the course of action is suitable for a client. The exact responsibilities of the two parties will depend on the nature of the services offered.

<sup>13</sup> In particular, Principle 6 (Customer's interests): A firm must pay due regard to the interests of its customers and treat them fairly; and Principle 7 (Communications with clients): A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

investment service should not be a default investment solution. Where the recommendation of a DIM is not a personal recommendation, a firm would not need to demonstrate that it has picked the DIM based on a comprehensive and fair analysis of the market. However, the firm should undertake sufficient due diligence on a DIM before recommending it to a client, so that it can make a judgement about whether it is the right solution for the client.

- 5.20 There may be circumstances in which a firm, by recommending a discretionary investment service, is in effect recommending a particular investment, for example if the adviser explicitly or implicitly recommends particular funds offered by a DIM. If this is the case, a recommendation to use a discretionary investment service would amount to a ‘personal recommendation’<sup>14</sup>, and the rules applicable to personal recommendations would apply, including those for independent advice. Another example of a personal recommendation is where an adviser recommends a retail investment product in which the underlying investment approach will be managed by a DIM. In this case, the DIM is integral to that retail investment product, and the advice to use the product and the DIM must be suitable and the suitability report should discuss the advice as a whole and explain all charges that apply to the client, including those for the DIM.
- 5.21 If a firm recommends a discretionary investment service to a client as part of a wider service, which includes advice on retail investment products, it should ensure that the advice on retail investment products meets the standard for independent advice.

## 6 Advisers

- 6.1 Personal recommendations on retail investment products are subject to the same standards, regardless of the adviser who provides them. We have been asked, however, to clarify how differences between the qualifications and skills of advisers may have an impact on the ability of advice to meet the standard for independent advice. This section covers the specialist activities of advising on pension transfers and pension opt-outs and advising on long-term care insurance contracts, as well as other ways in which advisers may be restricted in their scope.

### Recognised specialist activities

- 6.2 There are two specialist activities related to advising on investments that we currently recognise in our training and competence regime – these are:
- (a) advising on pension transfers and pension opt-outs; and

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<sup>14</sup> CESR Q&As on the definition of advice says that ‘Advice to become the client of a particular investment firm (e.g. a particular portfolio manager), or to use its services in a certain way, would need to relate to one or more specific financial instruments in order to be considered as investment advice under MIFID’. The definition of personal recommendation in our Handbook glossary broadly follows the MIFID definition of investment advice.

- (b) advising on long-term care insurance contracts.

### *Pension transfers and pension opt-outs*

- 6.3 A pension transfer specialist is defined in the Handbook as an individual appointed by a firm to check the suitability of a pension transfer or pension opt-out who has passed the required examinations. Pension transfers and pension opt-outs in this context are narrowly defined, relating to the transfer of deferred benefits from, or opt-out of, an occupational pension scheme in favour of a personal pension or stakeholder pension. A firm must have a separate permission to provide advice on pension transfers and opt-outs.
- 6.4 If a firm does not have permission to provide advice on pension transfers and pension opt-outs, it can still hold itself out as giving independent advice. This is because such a firm will not be constrained in its ability to provide advice on all types of retail investment products, as the definition of a retail investment product does not include occupational pension schemes. Although COBS 19.1G says that a firm should start by assuming a transfer or opt-out is not suitable, all competent retail investment advisers who give independent advice should be able to identify clients for whom a pension transfer or opt-out should be considered, and be in a position to refer clients to a third party if their firm does not have the appropriate permission or access to a pension transfer specialist.
- 6.5 A firm that gives advice on pension transfers and pension opt-outs may, in the context of this service, also give personal recommendations on personal or stakeholder pension schemes (which are retail investment products). If this firm is holding itself out as providing independent advice, it should ensure that such recommendations meet the standard for independent advice.

### *Long-term care insurance contracts*

- 6.6 Long-term care insurance contracts are retail investment products.<sup>15</sup> Advising on long-term care insurance contracts requires a specialist qualification, but not a separate permission. We do not expect a firm that holds itself out as providing independent advice to have an adviser who is qualified to advise on long-term care insurance contracts, because it is a niche market for which we currently require additional qualifications. But, as with pension transfers, all competent retail investment advisers who give independent advice should be able to identify clients for whom a long-term care insurance contract should be considered and be in a position to refer these clients on to someone who can provide advice on these products. Advisers should not recommend a product that is an alternative to a long-term care insurance contract, where a long-term care insurance contract would be suitable, because they have not passed the relevant examination.

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<sup>15</sup> Long-term care insurance contracts which meet the following definition are life policies:

A long-term insurance contract:

(a) which provides, would provide at the policyholder's option, or is sold or held out as providing, benefits that are payable or provided if the policyholder's health deteriorates to the extent that he cannot live independently without assistance and that is not expected to change; and

(b) where 'benefits' are services, accommodation or goods necessary or desirable for the continuing care of the policyholder because he cannot live independently without assistance.

#### Other adviser roles

- 6.7 A firm that holds itself out to all clients as providing independent advice should ensure that appropriate systems and controls are in place so that all personal recommendations in relation to retail investment products meet the standard for independent advice, including from inexperienced advisers or advisers who may wish to specialise in a particular area of investment advice (such as pensions). This is also the case if a firm wishes to put in place mechanisms, such as licensing of advisers, to control the quality of advice on certain investment products (such as higher risk products that are rarely going to be suitable for the firm's clients).
- 6.8 More than one adviser may be involved in developing independent advice for a client. An adviser may, for example, wish to consult an experienced colleague on a particular subject before delivering personal recommendations. Similarly, a number of people could be involved in product research and investment monitoring. It may be possible for a team approach to be adopted. However, if a retail client has contact with a number of advisers within a firm, there would need to be a mechanism in place to ensure that any resulting personal recommendation meets the required standard (for example, a particular adviser has oversight of all personal recommendations given to a particular retail client, to ensure that the standard for independent advice is met). To reiterate, it is the firm's responsibility to have appropriate systems and controls to ensure that personal recommendations provided by their advisers meet the required standard.
- 6.9 As outlined above, a firm that provides independent advice can refer clients for pension transfer advice or for advice on long-term care insurance products. Such firms can also make internal or external referrals for advice on non-retail investment products. If a firm does not provide any personal recommendations on retail investment products to a client, and refers them to another firm instead (for example, a firm that provides restricted advice), this will not affect its independent status. We would, however, expect firms to undertake sufficient due diligence on a service before recommending it to their clients to meet their obligation to treat customers fairly.