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The FSA's Proposed New Rules on Platforms

Platforms are internet-based services used by intermediaries (for example, investment advisers) as 'access points' to view and administer investments. They allow advisers to analyse a client's portfolio and choose products for their clients.

Introduction

The Financial Services Authority's (the "FSA") recent policy statement (PS 11/9) on platforms, *Delivering the RDR and other issues for platforms and nominee related services*, introduced several changes to the current rules on the use of platforms in an attempt to make markets more transparent for consumers and to provide a better service for the end investor. In particular, the FSA was concerned that the way fund platforms are currently paid may be detrimental to investors because:

- investors do not know how much a platform is being paid to sell different funds; and
- the platform may only offer funds that give rebates to platforms and/or consumers (which can create bias in favour of more costly products and potential mechanisms for advisers to receive commission).

The FSA's Policy Statement covers the following:

- defining a platform and distributing products through a platform, which includes definition of platform service and what the FSA expect of advisers when using a platform;
- payments to platforms and consumers, how platforms are paid and the adviser charging-related issue of rebating product charges to consumers;
- re-registration and capital adequacy, re-registration of a client's investments by a platform or other nominee company to another platform or nominee company, and the capital adequacy requirements for firms providing platform services; and
- investing in authorised funds through platforms and other types of nominee company and requirements to ensure that relevant fund information is passed to the end investor.

Overview of Key Changes

The FSA is hoping its proposed new rules will ensure:

- better service for consumers by requiring platforms and nominee companies to:
    - transfer assets held on behalf of consumers to another person quickly and efficiently, when requested (so that consumers can move their investments quickly if dissatisfied); and
    - pass on fund information to end investors; and
- greater transparency and efficiency in the market by:
    - requiring platforms to disclose to professional and retail clients any fees/commission they arrange to accept from third parties (e.g., fund managers or other product providers) in relation to retail

investment products, **in advance** of the platform providing services to that client; and

- requiring advisers using platforms to ensure that the platform services used present their products without bias.

The Main Changes in More Detail

Intermediate Unitholders ("IUs")

The definition of IUs has been changed to include all types of nominee companies (for example, ISA or SIPP providers holding units in funds on behalf of retail clients). (Discretionary investment managers will not be considered to be IUs, however).

IUs will now have obligations regarding the provision of information to end investors. In particular:

- they must forward certain documents and written notifications to end investors which they have received from Authorised Fund Managers ("AFMs") or fund depositaries;
- these documents can be forwarded on electronically (for example, an email summary of any changes with a hyperlink to details of those changes on an area of IUs website); and
- IUs must pass on short-form reports at least quarterly.

The new rules do not require IUs to facilitate the exercising of voting rights by end investors. Firms will be allowed to maintain the approach they currently take regarding voting rights; however, IUs must now provide more information to AFMs and end investors by:

- informing end investors of any Fund EGMs and certain details on the proposals being put forward; and
- providing aggregated information to AFMs at their request. (A number of IUs already do this, therefore, this may not be too burdensome).

Why have the changes been made?

- To prevent AFMs being distanced from the end investor, which is more likely now that the use of platforms has increased;
- to ensure investors are aware of changes when they are announced;
- to provide a better service to consumers; and
- to aid the logistics of providing the required information (regarding email communication).

Introduction of a Definition of a "Platform Service Provider" ("PSP") (and Deletion of the Definition of "Funds Supermarket Service")

The definition of a PSP is wider than the old definition of a "wraps/fund supermarket service"; therefore, more firms will be caught by the PSP provisions.

Who will fall within the definition of a PSP?

- Stockbroking firms providing execution-only trading services;
- equity ISA managers offering funds from different product providers; and
- wraps and fund supermarkets.

Who/what will fall outside the definition?

- Private client investment managers and advisers providing general administrative services;
- AFMs;
- SIPP operators;
- custodian activities; and
- services solely paid for by adviser charges.

What are the consequences?

- If a firm is considered a PSP, it will need to comply with the new rules in COBS 6.1E. These include presenting its products without bias and disclosing to clients any fees or commission it arranges to accept from a third party (such as a fund manager or other product provider).
- The new rules will make it increasingly difficult for independent firms/advisers to use a single platform for all clients and comply with COBS independence rules. It is unlikely that single platform featuring products which pay the platform a rebate will be deemed "suitable".

Platforms Facilitating Payment of Adviser Charges

Some adviser firms use cash accounts held on platforms to facilitate the payment of adviser

charges. Where this occurs, platforms will now have to adhere to the same standards as are required by product providers (COBS 6.1B.9). In particular:

- platforms must be satisfied that the client has agreed to the adviser charge and how it is carried out (for example, by receiving a copy of a form detailing any charges (signed by the client) which has been given to the product provider by the adviser); and
- this change is an attempt to ensure consistency across the industry once the Retail Distribution Review ("RDR") rules on facilitation come into force.

Expected Costs of the Changes to the Industry (Not Accounting for a Ban on Cash Rebates)

Type of Firm	One-off costs (£m)	Ongoing costs (£m)
Platform Operators	40.4	20.4
Fund Managers	2.9	0
Other IUs	12.1	28.0
Total	**55.4**	**48.4**

A Key Omission

The FSA's consultation paper on the new rules proposed a ban on both payments by product providers to platforms and cash rebates from product providers to investors. Under the current rules, some platforms can "bundle" charges for funds, advice and the platform into a single 'management' fee paid by the investor to the product provider. The provider can then rebate a portion of this fee to platforms and/or advisers to pay their charges. The fact that the cost split is not disclosed to investors and the potential compromise of independence (of the platform and the adviser) as a result of this practice has caused concern to both consumer representatives and the FSA itself.

However, the proposed rules do not include the bans, with the FSA citing potential "unintended consequences" and the requirement for further research as its reasons for delaying the introduction of any bans until 31 December 2012 at the earliest. Platform operators are (for the time being) breathing a sigh of relief; however, several financial services firms and the Financial Services Consumer Panel have expressed disappointment that, following years of consultation, no implementation date for such bans has been set.

Implementation of the New Rules

The changes set out above will all take effect from 31 December 2012, through the RDR (Platforms) Instrument 2011.

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