

Investment Platforms Market Study

A summary of the FCA's Final Report

Following the FCA's Interim Report looking into the platform market in the UK, the regulator published its final findings and remedies (MS17/1.3) in March 2019. The market study explored whether consumers can make informed decisions about the choice of platform, the investments they choose and whether firms compete to add value for consumers.

Reassuringly, the regulator found that the market is working well in many ways for both advised and non-advised consumers. However, the FCA has identified a few areas that need improvement along with some proposed remedies.

Below we briefly summarise the key points from the study, although we recommend firms read the [full text](#) to see how they may be affected.



The FCA's key findings and proposed remedies:

Shopping around between platforms

- Consumers need to be able to easily access, assess and compare information on non-price features and how much it will cost them to invest
- Consumers value the non-price features of platforms and the FCA does not have concerns about the ability of consumers to compare non-price features
- The FCA does still have concerns about the ability of consumers to shop around on the basis of price. It found that many consumers have low awareness of the charges they pay
- Most platforms have a large number of different fees and ways of setting prices. Charges can also be quoted in absolute terms or as a percentage. The use of different terms can make it difficult for consumers to identify and compare fees
- While the FCA has been encouraged by the way some firms are innovating in the way they present costs and charges information, it still found it difficult to find pricing information for a small number of advised platforms
- Overall, it can still be difficult for consumers to find all the relevant information to assess the cost of investing through a platform.

The FCA's final position

- All platforms need to comply with existing costs and charges disclosure requirements
- The FCA acknowledges and welcomes the initiatives of different firms and trade bodies to consider how to make this information simpler, clearer and more readily available to consumers
- The regulator believes this is not the time to introduce further changes to cost and charges disclosure requirements
- The UK Platform Group (UKPG) has committed to take

forward work to identify improvements to support consumer understanding and enable easier platform comparison

- The FCA expects firms to continue to reduce complexity and improve the clarity and availability of information on costs and charges
- The regulator will review industry progress in 2020/21. It will then consider appropriate regulatory intervention if needed.

Switching platforms

Improving the switching process

- The FCA wants to make the process easier for consumers who want to switch platforms, which can be expensive, complex and time consuming
- Switching involves several steps, each of which can involve several stages and delays
- The regulator hopes to see progress in the following areas:
 - o Improved standards for transfers and re-registration times with maximum timescales for each step in the switching process
 - o Clearer consumer communications from the receiving provider explaining the process and timelines, and giving a point of contact
 - o Publication of transfer times data so consumers and third parties can compare platform performance

- The FCA acknowledged the industry's efforts to improve the process. The Transfers and Re-registration Industry Group (TRIG) has published an industry framework which includes expectations for standards and communications
- TRIG launched 'STAR' in October 2018, a not-for-profit joint venture to develop and oversee the framework's implementation and monitoring.

The FCA's final position

- The regulator supports STAR's aim and work, given their framework is aligned to the FCA's desired outcomes
- Given progress and direction of travel to date, this industry initiative may prove the most timely, proportionate and cost-effective remedy to improve outcomes for consumers
- The FCA will review progress made later this year and, if needed, again in 2020 and take further action if required.

Exit fees

- Exit fees create a barrier to switching and also contribute to the complexity that affects consumers' understanding of costs and charges.

The FCA's final position

- The FCA thinks that there is a strong case for addressing platform exit fees for new business, as they act as a barrier to switching and reduce firms' incentives to deliver better services for all consumers
- The regulator has issued a [Consultation Paper](#) (CP19/12) on exit fees. It sets out the options for:
 - o How an exit fee should be defined
 - o The scope of the intervention
 - o Whether the intervention should be a ban or a cap on such fees (the FCA's view is that a ban on charges is likely to be more effective)
- The FCA invites views on CP19/12 by 14 June 2019 (responses can be sent to cp19-12@fca.org.uk).

Unit class conversion

- Discounted (or 'superclean') unit classes are typically created when a platform negotiates lower fund charges with a fund manager. When a consumer invested in these units wants to move their investment, it should be possible to do this on an in-specie basis without having to sell and repurchase units in the same fund
- Not all platforms facilitate such a conversion, instead requiring that the ceding platform either:
 - o Sells the units in the original unit class at a given valuation point. They then buy units in the new unit class at another valuation point prior to transferring to the receiving platform
 - o Sells the units and transfers the assets as cash. The receiving platform then rebuys the holdings in the new unit class

In both these cases, consumers may lose money due to market movement, unnecessary transactional costs and through potentially having to pay tax.

The FCA's final position

- The regulator has decided to consult on new rules requiring:
 - o Platforms to offer consumers the choice of transferring units in-specie where the same investment fund is available on both the ceding and receiving platform
 - o The ceding platform to take the necessary steps to bring about conversion of the units which the receiving platform can accept for an in-specie transfer (where the original share class is not available on the receiving platform)
 - o The receiving platform to offer consumers the option, as part of the funds transfer process, to convert units into discounted units (where they are available for investment by the consumer).

Advisers recommending a platform switch

- Advisers rarely recommend moving existing investments from one platform to another. It can be difficult to switch assets between platforms and many advisers charge clients an extra fee to cover administration and advice (on top of any ongoing advice fee).

The FCA's final position

- The regulator considers the main barrier to switching is the time and complexity of the switching process itself. It is, therefore, not proposing to issue additional guidance setting new expectations for advisers
- Advisers need to be able to demonstrate that their charges are fair. If ongoing advice charges do not cover the costs of assessing the benefits of switching, advisers need to be able to justify this.

Competition between adviser platforms

- Most services offered through adviser platforms benefit consumers either directly or indirectly. However, some platforms may provide services to advisers which may inappropriately alter their incentives
- The regulator also has concerns about the treatment of orphan clients. These clients may face restrictions in the platform services they receive or pay more for these services without reason.

Identifying orphan clients

- In its Interim Report, the FCA found platforms were not proactively monitoring whether clients continued to have a relationship with an adviser. Platforms responded stating that advisers typically notify them when a relationship ends. The risk of collecting advice fees from orphan clients is, therefore, low.

The FCA's final position

- There appears to be existing controls that sufficiently manage the risk of orphan clients continuing to pay advice fees. Advisers already have an obligation to ensure that they are not receiving fees from clients they no longer have a relationship with. The regulator also expects advisers to inform platforms where their relationship with a client has ended.

Supporting orphan clients

- In its Interim Report, the FCA said that orphan clients are unlikely to be well served by staying on adviser platforms, as their ability to access and alter their investments is usually restricted
- The regulator has undertaken work to gain a better understanding of how adviser platforms support orphan clients. Platforms typically engage with new orphan clients a number of times in the first few months after their relationship with their adviser ends, outlining their options and explaining any limitations
- Platforms also told the FCA that it is not always in the client's best interest to switch to a different platform
- The FCA found no evidence that orphan clients face additional barriers to switching to a new platform compared to clients with advisers or those on D2C platforms.

The FCA's final position

- Overall, the regulator agrees that it may not be in a client's best interests to switch to a D2C platform, particularly as orphan clients do not appear to face prohibitively restrictive services.

Orphan client charges

- In its Interim Report, the FCA found that some platforms charge orphan clients extra fees and these seem high
- In response, some platforms stated that these clients require extra support and are arguably more expensive to serve.

The FCA's final position

- The regulator accepts that there may be some additional costs for servicing orphan clients. However, these could be unfair where they do not reflect costs and clients get the same services their platform already offers
- Given only a small number of firms currently charge additional orphan client fees, the FCA is not introducing specific rule changes at this time. Instead, it will be following up with the individual firms and will intervene as appropriate.

Treatment of non-monetary benefits

- Certain services, including the provision of white-labelled solutions and certain training for advisers, might be caught by the inducement rules.

The FCA's final position

- Both platforms and financial advisers should continue to consider whether the non-monetary benefits they offer or receive are permissible under the inducement rules.

Informed investment choices

- As well as administering their investments, platforms can help consumers make informed investment choices and to get a better deal on funds. The FCA's expectation is that a well-functioning platform market should help consumers make informed choices between funds.

Presentation of fund charges

- The FCA thinks firms can improve the clarity and prominence of fund charges information. Firms should also take into account the findings of the MiFID II costs and charges disclosures review findings.

The FCA's final position

- After taking into account recent regulatory change and positive steps taken by the industry, the regulator is not taking forward further rules on disclosure of costs and charges at this time.

Promoting funds

- Promoting funds is one way in which platforms compete to attract consumers. Such promotions can potentially cause consumer harm. For instance, platforms that have 'in-house' funds have an incentive to promote them over third-party alternatives.

The FCA's final position

- Under FCA rules, vertically-integrated firms need to manage their conflicts of interest
- Best Buy lists have an impact on consumer choices and the regulator expects Best Buy lists to be constructed on an impartial basis
- The FCA believes that MIFID II, and the work taken forward by the industry, will help to further reduce the risk of harm.

Providing model portfolios

- Similarly-labelled model portfolios often have exposure to significantly different underlying assets and, therefore, experience different volatility in returns. There is potential harm if unhelpful naming conventions and inconsistent disclosure result in consumers making poor investment choices.

The FCA's final position

- For model portfolios structured as funds, work is currently underway to improve the disclosure and comparability of information. The FCA will wait until its changes are fully adopted before taking forward any further remedies.

Investing in securities

- Platforms are required by FCA rules to take steps to obtain the best possible results for their clients when executing trading orders.

The FCA's final position

- Platforms need to improve their order-handling procedures and conduct more comprehensive best-execution evaluations. This will result in better outcomes for retail clients
- Firms must take steps to obtain the best possible results for their clients when executing trading orders. The FCA will review whether firms are improving this and proceed with supervisory intervention as appropriate.

Holding large cash balances

- In its Interim Report, the FCA said that it had found that large cash balances accrue on platforms, and significantly more so on D2C platforms
- If consumers are holding high proportions of cash on a platform for long periods of time this could be of concern
- Further analysis suggests that much of the potential harm arising from money being held in cash – in terms of foregone interest and investment returns – arises from cash held in pension wrappers
- It is important that the charges for cash held and the interest rates paid are transparent to consumers. They can then shop around and place pressure on platforms to pass through interest and keep charges competitive.

The FCA's final position

- Cash held in pension wrappers is within scope of the FCA's [Retirement Outcomes Review](#). The regulator expects its proposed rules to reduce the harm arising from cash held in pension drawdown accounts
- Non-pension consumers typically make an initial choice to hold their money as cash and are less likely to accumulate persistently high cash balances
- The industry is working to agree a common model for describing and disclosing the treatment of interest on client cash and for calculating its effective cost to clients
- All these factors lead the FCA to conclude that the potential for harm from persistent large cash holdings on platforms outside pensions products is not significant enough to warrant intervention.

Entry, expansion and commercial relationships

- Challenger firms are an important source of competitive pressure for established businesses. In markets where challengers cannot enter or grow, established firms tend to be less responsive to consumers, less efficient and less innovative.

Fund discounts

- Some platforms secure discounts on fund charges and this creates benefits for consumers. Discounts are concentrated on the largest platforms, making it potentially harder for smaller platforms to compete
- The FCA found evidence of commercial arrangements where the fund manager commits not to offer lower fund charges on competing platforms – an example of 'most-favoured nation' clauses (MFNs)

- These MFN arrangements could have a negative impact on competition in the following ways:
 - If the funds cannot be offered at a lower price elsewhere, this may reduce another platform's ability to negotiate a discount
 - Such arrangements could make it more difficult for other platforms to enter the market or grow their market share
 - If funds cannot be offered more cheaply on other platforms, this may allow the 'MFN' platform to increase its fee above that of its competitors.

The FCA's final position

- The regulator found some MFN arrangements in the sector, but few concerns were raised by fund managers and platforms and the arrangements do not appear to be widespread
- The FCA reminds firms of their obligations to self-assess their commercial arrangements for compliance with competition law.

Other barriers to entry and expansion

- The FCA looked at whether there are other barriers that may prevent competitors from entering or expanding in the platform market. The barriers examined were economies of scale, technology, consumer acquisition, the cost of complying with regulation and the vertical integration of platforms with fund managers.

The FCA's final position

- The regulator sees consumer acquisition as the biggest barrier to expansion. The FCA believes its remedies to facilitate shopping around and switching should help reduce barriers to entry and expansion and make it easier for platforms to compete. It does not see the need for any other remedies.

FundsNetwork welcomes the FCA's final report

We believe the FCA's Final Report is good news for investors. The recommendations in the study are encouraging and the regulator recognises that the platform market is working well in many respects, with high consumer satisfaction.

FundsNetwork does not charge exit fees so we welcome the FCA's focus on ensuring that consumers are charged reasonably without penalties for transferring their assets. FundsNetwork is fully engaged with the TRIG initiative and the establishment of STAR. We are, therefore, very supportive of the FCA's attention on ease of switching between platforms. We believe that overall this happens relatively seamlessly between platforms, but we do need to apply focus on all firms offering retail distribution services, not just platforms.

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