The Assessing Suitability Review – Results

May 2017

Contents

How to navigate this document onscreen

returns you to the contents list

takes you to helpful abbreviations

1 Summary

Background

1.1 In planning for their financial future consumers often face complex and varied decisions. It is, therefore, essential that a well-functioning advice market for pensions and investment advice is there to support them. The suitability of advice is important for the financial advisory sector and advice was highlighted as one of the seven priorities in the Financial Conduct Authority's Business Plan 2016/17[1].

1.2 We initiated the Assessing Suitability Review (the review) in April 2016 in recognition of the important role we have to play supporting the sector in delivering suitable advice. The purpose of the review is to assess a statistically robust sample of advice files that allows us to draw conclusions on the suitability of advice and quality of disclosure in the sector as a whole.

1.3 The results from the review will:

- enable us to measure how the sector is performing
- identify any areas where the sector is meeting our rules and expectations
- enable us to communicate examples of good and poor practice
- enable us to focus our resource on firms and areas that pose a greater risk to customers
- assist us in measuring the impact on the sector of future regulatory interventions

Overall results

1.4 Our review assessed 1,142 individual pieces of advice given by 656 firms against the suitability and disclosure rules in the Conduct of Business sourcebook (COBS). We found the following in terms of suitability:

- In 93.1% of cases, the sector provides suitable advice
- In 4.3% of cases, the sector provides unsuitable advice
- In 2.5% of cases, the sector provides unclear advice[2]

1 www.fca.org.uk/publication/corporate/business-plan-2016-17.pdf
2 Our results are rounded to the nearest one decimal point, therefore they do not add up to exactly 100%.

1.5 We consider that these are positive results for the sector. We believe they are a result of the successful adoption of the Retail Distribution Review (RDR) by advisers and reinforced by our previous supervisory and enforcement activities.

1.6 While the overall results are positive, where we identify specific areas of advice which pose a higher risk to customers, we will consider focusing our resource on them. In our recently published Business Plan for 2017/18[3], we announced that we will carry out further work to target those firms providing unsuitable advice about complex products.

1.7 Our disclosure results were:

- In 52.9% of cases, the sector provides acceptable disclosure (i.e. our disclosure requirements have been complied with)
- In 41.7% of cases, the sector provides unacceptable disclosure (i.e. our disclosure rules have not been complied with)
- In 5.4% of cases, the sector provides uncertain disclosure

1.8 Our assessment of disclosure considers three distinct elements: the firm's initial disclosure, the product disclosure and the disclosure in the suitability report. Our results show that the main area where there is a high level of unacceptable disclosure is with firms' initial disclosure, which includes firms' costs and services. The overwhelming issues were: firms disclosing charging structures with wide ranges; and firms using hourly charging rates failing to provide an indication of the number of hours for the provision of each service, rather than firms failing to provide any cost information. The disclosure results demonstrate there is further work required in this area. We recognise firms' disclosure of product charges and the disclosure in suitability reports was regularly meeting our rules; however, some suitability reports were too long and/or complex. We consider disclosure to be an important aspect of the advice process as it assists customers in making informed decisions about their financial affairs.

1.9 We expect firms to consider the results, particularly those areas where we flag continuing concern, and consider whether there are any areas where they can improve.

Actions with firms

1.10 One of the opportunities presented by the review was that it enabled us to have direct contact with a large number of financial advisers. To improve accessibility for the firms involved, we set up a dedicated email inbox and phone line, and encouraged firms to use them where they had any queries or wanted to know more about what we were doing. We were encouraged that the firms involved were very engaged with the review, as demonstrated by the phone line receiving in excess of 1,000 calls from approximately 450 firms between April and September.

1.11 The review also provided an opportunity for the firms involved to receive our feedback. The firms involved received a letter in February 2017 detailing our findings from our review of their specific files. Where we identified any concerns, including weaknesses in

3 www.fca.org.uk/publication/business-plans/business-plan-2017-18.pdf

a firm's advice process, these were raised with the individual firm, and where relevant, the letters also highlighted areas of good practice.

Next steps

1.12 This report focuses on the results of the review and does not provide any examples of good and poor practice. This is because the report signifies the beginning of a communication programme which will run over the course of 2017 and into 2018. We will share more detail on our findings, including communicating examples of good and poor practice, throughout this communication programme. Having this on-going and developing communication approach will allow us to be more interactive and to use a variety of different methods to communicate including written publications, digital media and speeches. We will also build it into our future Live and Local programme of events[4].

1.13 Some important changes are coming to the advice and disclosure requirements through the Markets in Financial Instruments Directive II (MiFID II), the Packaged Retail and Insurance-based Investment Products regulation (PRIIPs) and the Insurance Distribution Directive (IDD). In a number of areas there will be increased requirements for financial advisers. Firms need to ensure that they take note of the new requirements and make any changes necessary.

1.14 We intend to repeat this review in 2019. This will be based upon advice delivered in 2018 and we will measure how the results have changed since 2015. This will also allow us to assess how firms have implemented the requirements introduced by MiFID II, PRIIPs and the IDD.

4 www.fca.org.uk/events-live-local

2 Methodology

Scope of the review

2.1 The review focused on pension and investment personal recommendations[5] delivered by firms to retail customers during 2015. It did not consider how firms meet our suitability rules when managing investments[6].

2.2 Each file review focused on a specific personal recommendation given during the relevant period. Our suitability assessment did not take into account other personal recommendations given to that customer at different points in time, nor did it consider future interactions with the customer.

2.3 Choosing the year 2015 as the relevant period allowed us to consider how advice was impacted by the changing landscape introduced by the pension reforms.

Statistical approach

2.4 The purpose of the review was to assess a sufficiently large enough sample of files to enable us to draw conclusions on the suitability of advice and quality of disclosure delivered by the sector as a whole. We engaged an external statistician to help us identify an appropriate sample of files and firms to include within the review.

2.5 Following statistical convention, we used a 95% confidence level throughout the review. The size of the confidence interval is affected by a number of factors, including the sample design and the size of the sample used.

2.6 For this review, we chose to target a confidence interval of +/– 3% around our estimates on the suitability advice and quality of disclosure for the whole sector. This means that we are 95% confident that the results for the whole sector fall within a range of +/- 3%[7] of our observed result. We also wished to estimate the level of the suitability of advice for three distinct advice areas with a 95% confidence level and a target confidence interval of +/- 5%. These three advice areas were:

a. investments

b. pension accumulation

c. retirement income

2.7 It is for this reason that the review involved us assessing 1,142 files from a selection of 656 advisory firms. We selected firms by allocating them to different groups (strata)

5 As defined in the FCA Handbook glossary: www.handbook.fca.org.uk/handbook/glossary/?starts-with=P.
6 As defined in the FCA Handbook glossary: www.handbook.fca.org.uk/handbook/glossary/?starts-with=M
7 The +/- 3% confidence is a target. However, the actual confidence interval will depend upon a number of factors, including our findings. Therefore the actual confidence intervals listed later in this report differ from the respective targets.

based upon size and selecting randomly from within the strata. The files were split broadly equally across all three advice areas. This provided us with the required level of statistical precision.

2.8 Further detail on our methodology is found in Annex I.

3 Suitability

Our approach

3.1 Our assessment of suitability is based upon the rules[8], guidance and principles[9] contained in the FCA handbook, as well as any published non-handbook guidance in existence at the time of the advice.

3.2 The focus of the suitability assessment was on whether the recommended solution was suitable for the customer. We recognise that the advice process may vary from firm to firm and that while we may identify weaknesses with an individual process; this does not necessarily lead to unsuitable advice and a poor customer outcome.

3.3 We assessed the suitability of advice for all cases and attached one of the following three ratings to each case:

1. Suitable
2. Unsuitable
3. Unclear[10]

Detailed results

3.4 Our results in relation to the sector for suitability are as follows.[11]

	Observed result	Lower confidence interval limit	Upper confidence interval limit
Suitable	93.1%	91.2%	94.7%[12]
Unsuitable	4.3%	3.1%	6.0%
Unclear	2.5%	1.7%	3.8%

Note: Figures rounded to the nearest one decimal point; therefore, they do not add up to 100%.

3.5 The positive results are encouraging and demonstrate that, in the main, firms in the sector are providing suitable advice.

8 COBS 9 (suitability)

9 Principle 6 requires a firm to pay due regard to the interests of its customers and treat them fairly; Principle 9 requires a firm to take reasonable care to ensure the suitability of its advice and discretionary decisions for any customers who is entitled to rely upon its judgement.

10 An unclear rating indicates that there was not enough information on file to evaluate whether the advice was either suitable or unsuitable. We consider an unclear rating to be a breach of COBS 9.2 as the firm has not taken reasonable steps to ensure the personal recommendation is suitable for the customer.

11 More detail is included in Annex 2.

12 For example, this means that we are 95% confident that the actual level of suitable advice delivered by the sector is between 91.2% and 94.7%.

3.6 While the overall level of unsuitable and unclear advice is low, our review tended to identify issues in two key areas:

1. *Risk profiling* – Where firms were not considering or mitigating the limitations of the risk profiling tool they used or where the recommended solution did not match the risk the customer was willing or able to take.

2. *Replacement business* – Where firms were recommending that customers give up valuable guarantees without good reason or where the additional costs appeared to outweigh the benefits of the recommended solution.

3.7 We encourage firms to consider the finalised guidance published on risk profiling[13] and on centralised investment propositions and replacement business[14] which specifically sought to address these issues. Should firms identify weaknesses with their approach, we expect them to consider what steps to take to address the issue identified and mitigate any risks going forward.

3.8 The statistical approach adopted enabled further analysis to identify any significant differences in the quality of advice provided by different segments of the sector. We identified the following statistically significant differences in respect of delivering suitable advice (i.e. statistically speaking, we are confident that the observed differences are real differences and not due to chance):

- Investment advice (94.8%) vs. pension accumulation advice (89.6%)
- Investment advice (94.8%) vs. retirement income advice (90.9%)
- Firms part of a network (97.2%) vs. directly authorised firms (91.4%)
- Independent (90.8%) vs. restricted (97.0%)
- Firms with 1-2 advisers (91.8%) vs. firms with 25 or more advisers (96.2%)
- Firms with 3-24 advisers (89.3%) vs. firms with 25 or more advisers (96.2%)

3.9 Given the relatively high level of suitable advice overall, and the relatively small differences between the above categories, we are not concerned by the differences identified. We intend to repeat this review in 2019 and will compare the results at that time against these results to help identify any trends.

3.10 We consider that there is limited scope for improvement by focusing our supervisory resource on the areas identified as showing statistically significant differences. Instead, we intend to focus on the root causes identified across all file types, namely risk profiling and replacement business. We will also use our supervisory resources to focus further on those areas where there might be a small number of firms that are giving rise to a high level of consumer detriment. In our 2017/18 Business Plan, we announced that we will carry out further work to target those firms providing unsuitable advice about complex products.

13 www.fca.org.uk/publication/finalised-guidance/fsa-fg11-05.pdf
14 www.fca.org.uk/publication/finalised-guidance/fg12-16.pdf

3.11 Our review also identified several examples of firms demonstrating good practice and going beyond compliance with our rules. This was evident across all three advice areas, including where firms gave retirement income advice and were having to deal with the significant change that came into effect in April 2015. Separately, we plan to feedback further detail on examples of good practice throughout our communications plan.

4 Disclosure

Our approach

4.1 Our disclosure assessment involved reviewing the files submitted against three different areas of our rules and guidance:

1. The initial disclosure of firms' charges and services – This is split across two stages: the generic disclosure and the customer specific disclosure[15]
2. The product disclosure[16]
3. The suitability report[17]

4.2 We also considered whether firms communicated to customers in a way that was clear, fair and not misleading[18].

4.3 We gave one of the following three possible ratings to a file when assessing disclosure:

1. Acceptable (i.e. our disclosure requirements have been complied with)
2. Unacceptable (i.e. our disclosure rules have not been complied with)
3. Uncertain[19]

Detailed results

4.4 Our results in relation to the sector for disclosure are as follows[20]:

	Observed result	Lower confidence interval limit	Upper confidence interval limit
Acceptable	52.9%	49.0%	56.8%[21]
Unacceptable	41.7%	37.9%	45.6%
Uncertain	5.4%	3.9%	7.5%

15 Detailed in COBS 6.1A (Adviser charging and remuneration) and COBS 6.2A (Describing advice services)
16 Detailed in COBS 14 (Providing product information to clients)
17 Detailed in COBS 9.4 (Suitability reports)
18 Principle 7 (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).
19 We rate disclosure uncertain when we can see evidence that a firm provided a document to the customer, but we did not receive a copy and are unable to complete an assessment.
20 More detail is included in Annex 3.
21 For example, this means that we are 95% confident that the actual level of acceptable disclosure delivered by the sector is between 49.0% and 56.8%.

4.5 This table provides the overall results. Therefore, it combines the results for all three areas of disclosure. This means that in 52.9% of cases, the sector provides acceptable disclosure in all three areas. In 41.7% of cases, at least one of the areas of disclosure is unacceptable.

4.6 We identified the following statistically significant differences in respect of providing acceptable disclosure (i.e. we are confident that the observed differences are real differences and not due to chance):

- Investment advice (56.7%) vs. pension accumulation advice (44.3%)
- Firms part of a network (69.0%) vs. directly authorised firms (46.0%)
- Independent firms (39.5%) vs. restricted firms (75.0%)
- Firms with 1-2 advisers (42.2%) vs. firms with 25 or more advisers (63.9%)
- Firms with 3-24 advisers (41.8%) vs. firms with 25 or more advisers (63.9%)

4.7 The statistically significant differences identified will enable us to target our communication programme to focus on the types of firms which deliver lower levels of acceptable disclosure. Any further communications material we produce, including examples of good and poor practice, will have these specific firm types in mind. In particular, we recognise that smaller firms may have less regulatory resources and will bear this in mind when designing any targeted communications.

4.8 It is important to note that our concerns are focused on certain areas of disclosure as detailed in the table below:

	Initial disclosure			
	Generic	**Customer specific**	**Product disclosure**	**Suitability report**
Acceptable	60.5%	82.6%	94.7%	92.8%
Unacceptable	34.0%	14.6%	3.2%	5.6%
Uncertain	5.5%	2.9%	2.1%	1.6%

Note: Figures rounded to one decimal point so not all add up to 100%.

4.9 Our review identifies that firms are broadly meeting our disclosure rules regarding the provision of product disclosure and the information that is required in the suitability report, although some suitability reports were too long and/or complex. The main area where there is unacceptable disclosure is the initial disclosure, specifically:

4.10 Firms disclosing an hourly charging structure but not providing an approximation of how long each service is likely to take.[22]

4.11 Firms using charging structures with a wide range.[23]

22 COBS 6.1A.20G(2)
23 COBS 6.1A.20G(1)

4.12 These are persistent issues, previously highlighted during the three stage RDR thematic review completed in 2014[24]. We are disappointed that this continues to be an issue. We consider that disclosure has an important role to play in supporting customers to make informed decisions about their financial affairs. Firms must ensure that their disclosure documents accurately reflect the services they provide and the associated costs.

4.13 However, whilst we are disappointed in the results regarding initial disclosure, our analysis suggests that there were only 6 files of the 1,142 we reviewed where the firm provided no information on the costs of the service to the customer.

24 www.fca.org.uk/publication/thematic-reviews/tr14-21.pdf

5 Next steps

5.1 We expect firms to consider the results, particularly those areas where we flag continuing concern, and consider whether there are any areas on which they can improve.

Communications programme

5.2 Following this publication, we will commence a communication programme that will run throughout 2017 and into 2018. This will look at the key areas where there is scope for improvement for the sector. These key areas include:

- Disclosure
- Replacement business
- Risk profiling and mapping to investment solutions

5.3 The purpose of the programme is to:

- provide further clarification on our expectations (we will communicate examples of observed good and poor practice)
- start a dialogue with firms about how best to work together to make improvements in the areas of concern

5.4 We previously published reports on all of these areas; therefore, the aim of the communication programme is to use a variety of methods over an on-going period of time to help embed our key messages within the sector.

5.5 Our intention is to make the communication programme flexible and tailored to meet the needs of the sector. To help us achieve this, we have asked all the firms involved in the review to provide suggestions on how we can best communicate with the sector.

Future supervisory work

5.6 We intend to repeat this review in 2019 and measure how the sector has responded to our findings and communications plan. This review will not only look at suitability of advice and compliance with our disclosure rules, but also compliance with any new relevant rules, including those under MiFID II, PRIIPS and IDD.

5.7 Our results provide a measure of the sector at a certain point in time. Therefore, repeating the review will give us more data on how firms are meeting our suitability and disclosure rules and will enable us to draw trends over time.

Annex 1
Detailed methodology

1. Section 2 of the report provides an overview of our methodology and the statistical approach we used. This annex provides further details on how we carried out the review.

2. We engaged an independent statistician to support us in creating a representative sample of firms and files to use to draw conclusions on the suitability of advice, and quality of disclosure, provided by the entire sector. To do this we estimated the size of the sector by using 'advice events'[25] as a proxy. This information allowed us to create a sample of firms to include in the review, and the number of advice events we would review for each firm across the three advice areas[26].

3. We contacted the firms in our sample to request:

i. A copy of their new business register for all pension and investment advice for 2015 – This was to allow us to select specific file(s) from the firm.

ii. Completion of a short online survey which confirmed the number of advice events by the firm, for the three advice areas, for 2015 – This allowed us to verify the data we held on the number of advice events for each firm.

4. Upon receipt of this information we selected the appropriate number of cases for each firm and advice type on a random basis[27]. This ensured that the review was not skewed by focusing on particular types of advice.

5. For the majority of firms involved in the review we requested only one file. This reflects the make-up of the sector which has a large number of small advisory firms. A greater number of files were selected from firms that represent a larger proportion of the sector. The file request sample is set out in the table below:

No. of files requested	No. of firms
1	481
2	94
3 - 4	50
5+	31

6. Once we received the requested files, we reviewed the advice and disclosure using our standard file assessment methodology. This is the same methodology we use as part of our business as usual supervisory approach. We carried out risk-based quality assurance to help ensure the accuracy of our results. As part of our quality assurance process, we sent detailed findings to each firm and asked them to comment on any factual inaccuracies in our findings. We received comments from 119 firms which led to a change in our findings for 35 firms.

25 By 'advice event' we are counting each individual piece of advice on a solution, delivered by a firm, as a single advice event.
26 Investments, pension accumulation and retirement income.
27 We ensured the basis was random by totalling the number of relevant advice events for the firm in 2015 using the new business register and then used a random number generator to select the specific file(s).

7. We assessed the entire file provided to us to come to a conclusion on the suitability of advice and quality of disclosure. This included looking at the 'know your client' information, assessment of risk, meeting notes, research and due diligence and the suitability report, alongside any other information the firm considered relevant to support the advice provided.

8. We aggregated the results from the individual file reviews to form what we called our 'nominal results' for the sector. However, to draw statistical inferences on the sector as a whole, we had to convert these 'nominal results' to what we call 'weighted results'. These weightings were applied to adjust for planned over and under-representation of our sample in two areas:

   i. Our sample included a broadly equal split of investment, pension accumulation and retirement income advice. This was to target the +/- 5% confidence interval for each of these advice areas. In practice, there is not an equal split of advice across these areas within the sector as a whole; therefore, a weighting was applied to bring the split between the different advice areas into line with the actual advice provided by the sector.

   ii. All firms in the sector were put into groups based on their total number of advice events. We then weighted the results to ensure they were representative of the sector.

9. Throughout the review process we have continued to liaise with the independent statistician to ensure our overall methodology, approach and results are robust from a statistical perspective.

Annex 2
Suitability findings

1. We highlighted the statistically significant differences in section 3. For all other comparisons, where there is no statistically significant difference, it is possible that there is no 'real' difference in the results for the sector.

			95% confidence interval	
			Lower bound	Upper bound
All Files				
All	Suitable	93.1%	91.2%	94.7%
	Unsuitable	4.3%	3.1%	6.0%
	Unclear	2.5%	1.7%	3.8%
File Type				
Investment	Suitable	94.8%	91.0%	96.7%
	Unsuitable	3.8%	2.2%	6.3%
	Unclear	1.4%	0.6%	3.3%
Pension accumulation	Suitable	89.6%	86.0%	92.4%
	Unsuitable	5.5%	3.6%	8.3%
	Unclear	4.9%	3.0%	7.9%
Retirement income	Suitable	90.9%	87.3%	93.6%
	Unsuitable	5.1%	3.3%	8.0%
	Unclear	3.9%	2.2%	6.8%
Firm type				
Firms within networks	Suitable	97.2%	94.2%	98.7%
	Unsuitable	1.6%	0.5%	4.7%
	Unclear	1.2%	0.4%	3.2%
Directly authorised firms	Suitable	91.4%	88.8%	93.4%
	Unsuitable	5.5%	3.9%	7.7%
	Unclear	3.1%	2.0%	4.9%
Scope of advice				
Independent	Suitable	90.8%	87.9%	93.0%
	Unsuitable	5.9%	4.1%	8.3%
	Unclear	3.3%	2.1%	5.2%
Restricted	Suitable	97.0%	94.4%	98.4%
	Unsuitable	1.8%	0.8%	4.2%
	Unclear	1.2%	0.5%	2.9%

Number of advisers at the firm				
1 - 2	Suitable	91.8%	87.9%	94.6%
	Unsuitable	5.1%	3.3%	7.9%
	Unclear	3.0%	1.3%	6.7%
3 - 24	Suitable	89.3%	84.8%	92.5%
	Unsuitable	7.7%	5.0%	11.8%
	Unclear	3.0%	1.6%	5.7%
25 or more	Suitable	96.2%	93.6%	97.8%
	Unsuitable	1.7%	0.7%	4.0%
	Unclear	2.0%	1.0%	4.0%

Note: Figures rounded to one decimal point so not all add up to 100%.

Annex 3
Disclosure findings

1. We highlighted the statistically significant differences in section 4. For all other comparisons, where there is no statistically significant difference, it is possible that there is no 'real' difference in the results for the sector.

			95% confidence interval	
			Lower bound	Upper bound
All Files				
All	Acceptable	52.9%	49.0%	56.8%
	Unacceptable	41.7%	37.9%	45.6%
	Uncertain	5.4%	3.9%	7.5%
File Type				
Investment	Acceptable	56.7%	51.1%	62.2%
	Unacceptable	37.4%	32.2%	43.0%
	Uncertain	5.8%	3.7%	8.9%
Pension accumulation	Acceptable	44.3%	38.9%	49.8%
	Unacceptable	51.3%	45.8%	56.7%
	Uncertain	4.5%	2.8%	7.1%
Retirement income	Acceptable	50.8%	45.4%	56.3%
	Unacceptable	43.9%	38.5%	49.3%
	Uncertain	5.3%	3.4%	8.3%
Firm type				
Firms within networks	Acceptable	69.0%	61.5%	75.6%
	Unacceptable	29.0%	22.6%	36.4%
	Uncertain	2.0%	0.7%	5.7%
Directly authorised firms	Acceptable	46.0%	41.5%	50.6%
	Unacceptable	47.1%	42.6%	51.6%
	Uncertain	6.9%	4.9%	9.6%
Scope of advice				
Independent	Acceptable	39.5%	34.8%	44.3%
	Unacceptable	53.8%	49.0%	58.6%
	Uncertain	6.7%	4.6%	9.7%
Restricted	Acceptable	75.0%	68.7%	80.3%
	Unacceptable	21.8%	16.8%	27.8%
	Uncertain	3.2%	1.6%	6.3%

Number of advisers at the firm				
1 – 2	Acceptable	42.2%	34.6%	50.1%
	Unacceptable	53.1%	45.2%	60.8%
	Uncertain	4.8%	1.9%	11.5%
3 - 24	Acceptable	41.8%	35.7%	48.2%
	Unacceptable	49.4%	43.1%	55.7%
	Uncertain	8.8%	5.7%	13.2%
25 or more	Acceptable	63.9%	58.0%	69.5%
	Unacceptable	32.8%	27.3%	37.9%
	Uncertain	3.3%	1.8%	6.0%

Note: Figures rounded to one decimal point so not all add up to 100%.

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