

For authorised corporate directors, fund managers and platform providers

Firms helping to run distributor-influenced funds

The factsheet reflects our current rules and has been updated to explain our expectations as a result of the Retail Distribution Review (RDR).

There are no rules which relate specifically to distributor-influenced funds: the factsheet provides guidance on rules which have a more general application. Some of the observations we make in this factsheet will therefore also be relevant to other investments.

What are distributor-influenced funds?

Distributor-influenced funds are created for the clients of a particular distributor, typically an adviser firm or network. They could be designed on a bespoke basis for the distributor or they could be set up using an existing fund that is tailored for the distributor. Fund administration and management is outsourced to other firms but the distributor may have a degree of influence over the fund (short of day-to-day asset selection). It may be, for example, that the distributor is able to:

- influence the hiring (or removal) of the Authorised Corporate Director (ACD) or the delegated investment manager or
- create accountability of the investment adviser by attending investment committees

They are commonly arranged as OEICs (where they may be known as broker OEICs, distributor funds or distributor-owned funds) but may also take other structures (like unit trusts or insurance funds). We have chosen to refer to them as 'distributor-influenced funds' in this factsheet, as this term covers the full range of possible structures.

In this factsheet, distributor-influenced funds are distinct from the operations of fund managers, collective investment scheme operators and private client investment managers for whom investment management is central to the business proposition. They are arranged by firms that have chosen to outsource to professionals as their preferred route, potentially without permission to manage investments or operate a fund.

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You should take into account that many distributors entering this market may not have practical experience in it and that the product presents different risks to those to which the distributor and its customers are ordinarily exposed.

Issues to consider

You may want to review your business processes to help distributors manage the challenges of offering these funds. It remains your responsibility to identify the issues that will be relevant but the following are some areas that you will want to consider.

Marketing the proposal to distributors

Promotional material to distributors should present a balanced view of the product, including the risks of the product and its disadvantages, to help advisers assess suitability for their clients. The fund prospectus, for which the ACD is responsible, should set out the relationship between the various parties, the extent of the distributor's decision-making powers, and the charging arrangements if payments are made out of scheme property.

Assessing commercial viability

Before launching a new fund, you should assess whether it will be commercially viable based on realistic assumptions and without compromising the adviser's obligation to provide suitable advice to each client (a contingency plan is needed in case funds do not achieve commercial viability).

Due diligence

A related matter is your assessment of whether to work with a particular distributor at the outset and regularly reviewing this decision (considering, for example, areas such as their training and competence, conflicts of interest procedures and TCF programme).

The appropriate level of distributor influence

It is important to decide the appropriate level of influence that you will accept from the distributor and to keep a clear distinction between the regulated activities each party is expected to perform. This is especially important if you are the fund's ACD because you have the ultimate regulatory responsibility for operating it compliantly, regardless of your commercial relationship with the distributor.

Product design and market research

Where relevant, you should consider work done to identify the target market and its needs, and whether the fund's charges are appropriate for expected returns (particularly for lower risk strategies where lower, more stable returns are targeted and higher charges would have a greater impact). There may be a reduction in yield (for products) or total expense ratio (for funds) above which you no longer expect this product to be suitable.

Communications with clients

It may be that you are better placed to produce standardised product disclosure material than distributors who are not normally required to produce this information.

Non-advised sales

Given the complexity and potentially high costs of these funds, it is unlikely to be fair to allow non-advised sales methods of distributor-influenced funds. Where relevant, if you wish to allow non-advised sales methods, you need to consider how this could be done in an acceptable manner.

Default funds

For similar reasons, it is unlikely to be fair to allow distributor-influenced funds to be sold as default funds. Where relevant, if you wish to allow them to be used as default funds, you need to consider how this could be done in an acceptable manner.

We note that many advisers are involved in choosing the default fund from an existing range for group personal pension plans. We do not regard this as falling within the scope of this factsheet.

Changes as a result of the Retail Distribution Review

Firms advising on distributor-influenced funds can not receive a share of product charges as remuneration. This means that you cannot pay a share of the annual management charge to them for their role on a fund governance committee.

Questions to consider

1. How will you promote distributor-influenced funds to distributors?
2. What due diligence will you conduct?
3. How will you assess how the design of the product meets the needs of the end client?
4. Will you allow non-advised sales or the funds to be used as the default option on a product?
5. What will happen if the fund does not reach commercial viability within an acceptable period?
6. How will you monitor funds to assess whether changes are necessary or whether different parties are performing the regulated activities for which they are responsible?
7. How will you assess whether the impact of higher charges on expected returns is acceptable?

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