Investment Platforms Market Study
Interim Report

Market Study
MS17/1.2

July 2018

How to respond

We are asking for comments on this report by 21 September 2018

You can send them to:

Kate Blatchford-Hick
Competition Division
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

Telephone:
020 7066 8794

Email:
investmentplatformsmarketstudy@fca.org.uk

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1 Executive summary

Introduction

1.1 Platforms are a relatively new but significant and growing distribution channel. The platform service provider market has doubled since 2013 from £250bn to £500bn assets under administration (AUA). This growth in AUA has been driven by rising markets and increasing levels of investment. More consumers are using platforms, with an increase of around 2.2 million more retail customer accounts between 2013 and 2017.[1] Platform revenue from retail consumers reached £1.3bn in 2017, up from £750m in 2013.

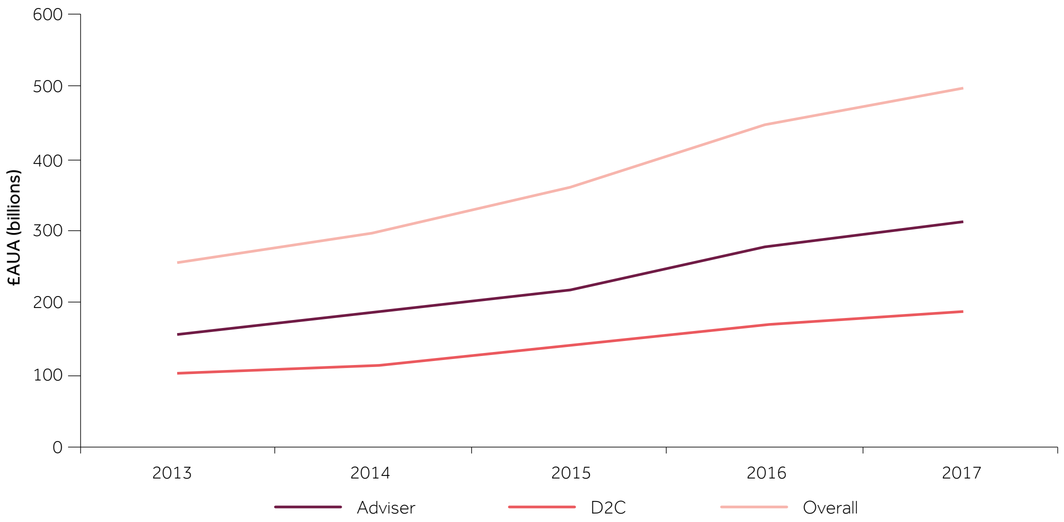
1.2 There are 2 main types of investment platform. Direct to Consumer (D2C) platforms collectively administer £189bn and are used by consumers without the help of a financial adviser. Adviser platforms collectively administer £311bn and are chosen by advisers but are paid for by consumers. Despite some new entry, the D2C market remains concentrated, with a single platform having a market share slightly higher than 40%. In the adviser market none of the top 4 platforms achieves a 20% market share and their market shares have changed in recent years.

1.3 Our market study looks at how competition is developing in this growing sector. Retail investors and financial advisers use investment platforms to access suppliers in one place, to execute, review and change their investments. Platforms can play an important role in the value chain by encouraging asset managers to compete for business. We wanted to assess the extent to which platforms are competing to deliver these benefits in practice.

1.4 In this report we explain our findings and the way we want to see the market develop. We welcome your comments.

1 FCA data. Just over a third of consumers appear to be using more than 1 platform and hence have multiple accounts.

Figure 1.1: AUA on platforms 2013 to 2017



Source: FCA calculations based on firm data.
Notes: Figures from 2013 to 2016 refer to year-end stocks. Figures for 2017 refer to the stock at end of June.

What did we find?

1.5 We found a mixed picture. The market appears to be working well in many respects, for both advised and non-advised consumers, and customer satisfaction is currently high. Consumers who pay more for their platform tend to get greater functionality on average. However, we are concerned that competition between platforms is not working well for 5 groups of consumers.

- **Switching between platforms can be difficult.** Consumers who would benefit from switching can find it difficult to do so.
- **Shopping around can be difficult.** Consumers who are price sensitive can find it difficult to shop around and choose a lower-cost platform.
- **The risks and expected returns of model portfolios with similar risk labels are unclear.** Consumers using these model portfolios may have the wrong idea about the risk-return levels they face.
- **Consumers may be missing out by holding too much cash.** Consumers with large cash balances on D2C platforms may not know they are missing out on investment returns, the interest they lose or the charges they pay by holding cash in this way.
- **So-called "orphan clients" who were previously advised but no longer have any relationship with a financial adviser face higher charges and lower service.**

In addition, the positive impact of platforms on competition between asset managers may be reduced because:

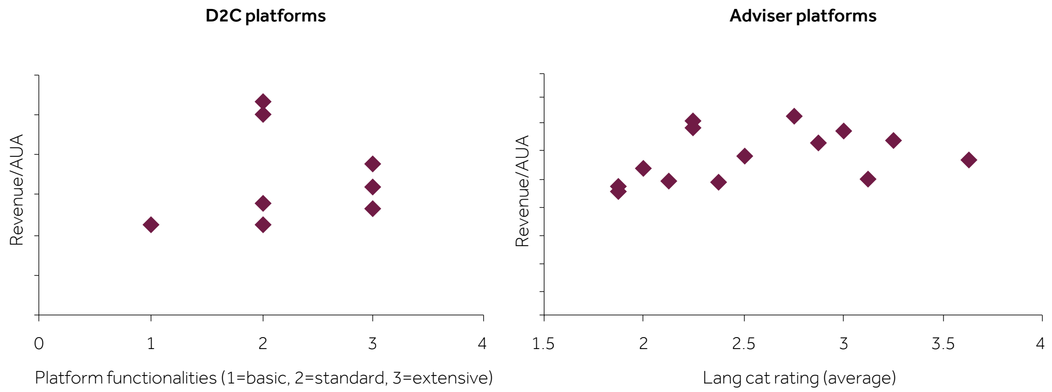
- Platforms employ commercial practices which may restrict fund managers' incentives or ability to offer fund discounts to competitor platforms, and this may reduce competition on fund discounts.

- Platforms could improve how they present fund charges at different stages of the consumer's decision making.

Platforms are popular with investors, and competition is working well in some areas

1.6 Users of D2C platforms care about price and other features of platforms, including the product range and ease of use. On average, consumers who pay more get more functionality in return. We have not observed widespread instances of consumers paying more for no good reason. Platforms also compete to provide services that consumers use and value, including access to a wide range of investments and tools to help them manage their investments.

Figure 1.2: Relationship between price and non-price features offered by platforms



1.7 Advised platforms compete by offering services to advisers, but are paid for by consumers. Most of these services benefit consumers, although we have outlined some exceptions below.

1.8 Platform financial performance does not suggest widespread competition concerns in the market. We do not find sustained excess profitability on aggregate in this market, and many platforms are loss making.

Switching between platforms can be difficult. Consumers who would benefit from switching can find it difficult to do so

1.9 The switching process for investors is complex and time consuming. Almost half of consumers who have not switched nor considered switching platform are happy as they are. But we found that 7% of consumers have tried to switch at some point but failed mainly because of the time involved, the complexity of the process and exit fees. We are not concerned about the rate of switching per se, what matters is the ability to switch – consumers should have the option even if they choose not to use it.

1.10 The time it takes to switch between platforms varies considerably. Switching is generally completed in a couple of weeks to a few months, but can take longer. We think barriers to switching are significant and could limit competitive pressure on platforms. Without this there is no pressure on providers to offer good value.

1.11 Advisers update their platform lists for new investments over time, but not many advisers switch existing investments as the process is complicated. This means that even if there are better options, which advisers use for new clients, they rarely switch existing investments across platforms. Many advisers in our sample charge an extra fee for switching on top of their ongoing advice fee, which can cancel out the potential benefit of lower platform fees and act as an additional barrier.

1.12 We think that improving the switching process will encourage more competition and benefit all consumers.

Shopping around can be difficult. Consumers who are price sensitive can find it difficult to shop around and choose a lower-cost platform

1.13 39% of non-advised consumers who have invested through platforms told us they choose a platform based on the price they will be charged. However, we have found that there are low levels of shopping around, with most non-advised consumers not shopping around or remembering doing so. Despite their stated importance, awareness of platform charges is fairly low with 29% of consumers either not knowing whether they pay charges for investing via a platform or thinking they do not pay any. Our consumer research suggests consumers are least satisfied with charges. We have also found that the most price sensitive consumers do not appear to be choosing the cheapest platforms more often than other consumers.

1.14 It is currently difficult for consumers to choose a D2C platform on the basis of price. It is not easy to find pricing information on platform websites. Most platforms also have a large number of fees, different pricing structures and different ways of setting prices, for example, in pounds or as a percentage of the investment amount. Inconsistent language makes it even harder to identify and compare similar fees across platforms. Different charging structures can in principle reflect different consumer needs and usage patterns. However, the level of complexity appears to go beyond catering for this, and we are concerned by both complexity and the lack of transparency.

1.15 Platform fees vary so it is important that customers understand what they are paying. For example, charges on a pot of £5000 investing in stocks and shares ISA can vary from 20 bps to 240 bps, with a potential £650 difference in returns over a 5 year period (assuming a 5% growth rate).

1.16 The MiFID II cost disclosure provisions should help consumers compare the total cost of investing.[2] However, there is scope for further improvement in how firms present the information mandated by MiFID II to consumers.

The risks and expected returns of model portfolios with similar risk labels are unclear. Consumers or their advisers looking for a particular risk level portfolio may have the wrong idea about the risk-return levels they face

1.17 Around 17% of non-advised consumers use the ready-made portfolios their platforms offer. These consumers tend to be the less active platform users, younger and less affluent investors. Platforms, alongside wealth and asset managers, are increasingly offering their own multi-asset and multi-manager funds and model portfolios to cater for this group of consumers. There has been steady growth in the model portfolios offered by platforms, with in-house model portfolios investments increasing from £5bn in 2011 to £38bn in 2017.

1.18 We have found that the information platforms provide about similarly labelled model portfolios makes comparison difficult. Similarly labelled model portfolios expose investors to very different underlying assets and volatility in returns.[3] We also found that model portfolio fees vary significantly, with higher fees resulting in lower risk-adjusted net returns on average.

2 The Packaged Retail and Insurance-based Investment Products (PRIIPs) regulation and the Insurance Distribution Directive (IDD) also introduce new costs and charges disclosure requirements.

3 Our total sample was 797 risk targeted model portfolios. 17% of the AUA in these portfolios from D2C platforms and 34% for adviser platforms had comparable risk labels.

Consumers may be missing out by holding too much in cash balances

1.19 Consumers using D2C platforms hold large cash balances. In 2017 they held £16bn in cash, amounting to 8.8% of AUA compared to 3.9% of AUA on adviser platforms.[4] Even where consumers make a conscious choice to hold cash they may not realise the cost of doing so through platform fees charged on their cash balance, potential lost investment returns, or potential foregone interest.

So-called "orphan clients", who were previously advised but no longer have any relationship with a financial adviser, face high charges and low service

1.20 We estimate that there are currently just over 400,000 orphan clients with just over £10bn of assets on platforms. The figure is rising. Life companies and asset managers also have orphan clients.

1.21 We have 2 main concerns. Orphan clients have limited ability to access and alter their investments on an adviser platform so are paying for functionality that they cannot use. While many platforms told us that they encourage orphan clients to find a new adviser or switch to a D2C platform, some platforms also charge orphan clients extra fees, of up to 0.5% on top of their pre-existing platform charges.[5] We estimate that around 10,000 orphan clients are currently paying extra fees amounting to over £1.2m every year.

Certain commercial practices may dampen competition on fund discounts

1.22 Consumers benefit when platforms negotiate discounts on investment charges from fund managers. The amount held in discounted funds[6] has increased since 2013 (£22bn to £47bn).

1.23 Discounts are concentrated on the largest platforms, making it potentially harder for smaller platforms to compete. To some extent, this is to be expected. Asset managers would rather offer discounts to larger platforms capable of attracting larger flows into their funds. Beyond this, however, we have observed arrangements between a small number of platforms and asset managers which could affect pricing of funds on other platforms. Under the arrangements asset managers offer these platforms the cheapest price in the market or prices no worse than on other platforms. This means that in principle fund managers may lack incentives to offer discounts to firms without these arrangements. We welcome views on these arrangements.

Platforms could improve the presentation of fund charges to consumers and financial advisers at relevant points in the consumer journey, which would strengthen competition between asset managers

1.24 Platforms generally do not appear to show advisers the individual and weighted average fund charges their clients are paying when they view client accounts. This means that, even if advisers are assessing fund charges from 3rd parties when selecting funds, platforms are not facilitating advisers' ongoing assessment of whether the client is receiving good value for money from their portfolios.

1.25 Adviser platforms could help advisers monitor whether their clients are receiving good value for money from their portfolios by showing the fund charges their clients are paying when they view client accounts. Some D2C platforms do not make it clear that fund charges may apply when they summarise the charges consumers will pay.

4 Figures are as at June 2017.
5 In most cases they also lose any discounts negotiated by their previous adviser.
6 Discounts are defined as the price difference between discounted and non-discounted funds on platforms. Most of the fund discounts on adviser platforms were secured before 2014, ie pre-RDR.

Our behavioural research suggests ways of presenting fund charges which encourage consumers to take them into account.

1.26 We think platforms can make fund charges more salient which will encourage competition between asset managers.

Potential areas of non-compliance with existing rules

1.27 We found that some advisers use services including the provision of some adviser education and training courses, white labelling, and bulk rebalancing and model portfolio management tools, which are likely to benefit advisers but not necessarily their clients. Some of these services are likely to be so-called non-monetary benefits, so they likely to be caught by our inducement rules. Advisers need to demonstrate that these benefits are acceptable minor non-monetary benefits, for example because they can enhance the quality of the service to the client and will not impair the firm's compliance with its duty to act in the client's best interests.

1.28 Most D2C platforms do not have robust Best Execution monitoring and many make it difficult for clients to know when their trade will be placed.[7]

Interim proposals on remedies

1.29 Competition between investment platforms can and should work better for consumers. We are keen to hear from stakeholders as we develop our thinking on what action to take to address the issues we have found.

1.30 We are open at this stage of the process to hear what measures may solve the problems we have identified. New rules introduced under MiFID II may provide an answer to some problems, however we may need to make additional rules or industry bodies may come forward with solutions to supplement the current regulations.

Help for consumers on D2C platforms who find it difficult to shop around and choose platforms on the basis of price

1.31 The information platforms provide can help consumers make good decisions about their choice of platform, products on the platform and the total cost of investing.

1.32 MiFID II has introduced aggregated total charge disclosure, which should help improve comparability. We are conducting a supervisory review to assess whether providers and distributors are providing the information required by MiFID II and PRIIPs. We will incorporate our findings on transparency and complexity with this review to assess whether these issues are due to non-compliance with MiFID II.

1.33 We are not proposing additional costs and charges disclosure rules at this stage. Yet we want to see more innovation in the way platforms present their MiFID II costs and charges data. This will help consumers to assess and compare the total cost of investing, for example by providing customers with interactive tools to calculate and personalise total charges, and to better raise awareness of fund charges.

1.34 Between our interim and final reports we will assess how industry is innovating while complying with the costs and charges disclosures in MiFID II which came into force

7 Please see Chapter 9 for a summary of the rules of Best Execution.

on 3 January 2018. We will then see if we need to introduce further remedies to make sure industry uses the opportunity created by MiFID II to genuinely help consumers compare and choose platforms.

1.35 Alternative options include requiring platforms to give intermediaries more data on platform charges and performance. They also include open data solutions where customers can export their usage history (including trading patterns, pot sizes and information about their funds) to third parties. We are interested in stakeholder feedback.

Measures to strengthen the extent to which platforms drive competition between asset managers

1.36 Platforms can play an important role to increase competition between asset managers. We have found that a small number of large platforms have arrangements to secure the best or no worse price from asset managers. We welcome stakeholder views on the positive and negative impact of such arrangements.

1.37 Our behavioural research suggests that by presenting charges in a clear, understandable and prominent way, platforms and other intermediaries can increase the attention investors pay to charges.[8] This could create more competition between asset managers. Platforms may wish to consider the findings from our research when they design the frameworks for consumer decision making so consumers can make informed choices between products. Between our interim and final reports we will assess how industry is innovating while complying with the costs and charges disclosures in MiFID II before introducing further remedies to improve the salience and comparability of fund charges.

Measures to help consumers building large cash balances without knowing about interest, charges and potential investment returns

1.38 To help consumers who have large cash balances but don't understand the cost or implications for expected returns, we will assess whether existing rules on disclosure[9] go far enough or whether further rules or guidance is required[10] to ensure our policy objective – to ensure consumers are making informed decisions – is achieved.

Measures to make it easier for investors and advisers to switch platforms

1.39 Following discussions with Supervision, in February 2016, the industry established the Transfers and Re-registration Industry Group which is currently taking forward an initiative to improve the switching process and reduce transfer times.[11] At a minimum, this should provide:

- **end-to end standards for transfer and re-registration (also known as in-specie) times through** the introduction of a maximum timescale for each step in the switching process

- **clear communication to customers** provided by the receiving provider at the start of the switching process detailing the transfer process, timelines and giving them a point of contact if they have any questions or wish to complain

8 Occasional Paper No. 32 Now you see it: drawing attention to charges in the asset management industry

9 In our view, the rule in CASS 7.11.32R is likely to be applicable to firms; if firms believe that the rule is not applicable to their business we would like to hear why they think this.

10 For example, rules in place for SIPP providers which require retained interest to be treated as a charge. See COBS 13 Annex 3 1.1R(4) and 1.2AR

11 The TRIG group published an industry framework 29 June 2018 available at: https://www.abi.org.uk/products-and-issues/lts-public/issues-in-long-term-savings/improving-transfers-and-re-registrations/

1.40 We welcome views on how the FCA can reinforce the industry initiative. One way we could do this is to use the minimum standards for transfers developed by the industry for the purpose of assessing whether firms are complying with the re-registration requirements of retail investment products in COBS 6.1G.1R. This rule requires reregistration requests have to be made 'within a reasonable time and in an efficient manner' as required by COBS 6.1G.

1.41 A further positive step would be for industry to **publish data on transfer times** so consumers and third parties can compare platform performance and put pressure on platforms to make improvements.

1.42 We expect the industry to implement changes in these 3 areas by the time we publish our final report in the first quarter of 2019. If we are not satisfied with the progress that has been made by that point, we will consider the merits of taking further action to improve the switching process. Our potential options include remedies to shine a light on firms' switching times and mandating timelines for the process.

1.43 Alongside supporting the industry initiative, we are also considering the following measures to reduce switching costs:

- banning exit fees
- improving switching between share classes, for example by requiring the ceding platform to switch consumers to the receiving platform's share class before a switch takes place

1.44 We are considering whether to issue more guidance to clarify our expectations for adviser charging for switching platform. Many advisers told us that they charge additional advice fees for switching platform because it is a full advice event which requires them to produce a suitability report. We recognise advisers need to be fairly paid for their work. But it is not clear to us why meeting suitability requirements to switch platforms should outweigh the benefits of switching platform.

1.45 We welcome stakeholder views on what additional work is required to meet suitability requirements above the ongoing suitability assessment.

Measures to help orphan clients

1.46 To improve outcomes for orphan clients we are considering the following measures:

- tackling price discrimination between orphan and existing clients
- requiring platforms to have a process in place to get these customers to switch to a more appropriate proposition
- requiring adviser platforms to check, if there is no activity after a year, that their customers are receiving an advice service, and inform the FCA of orphan clients who are still paying an adviser for advice they no longer receive

Measures to help consumers who may be exposed to unexpected risk levels

1.47 We recognise that the issues we have identified with in-house model portfolios might also apply to portfolios provided by wealth and asset managers and more to particular types of platforms. We will do further work between our interim and final reports to assess the scope of these issues.

1.48 Depending on what we find, we could then explore measures to help consumers make better choices between model portfolios. These could include, for example, the disclosure requirements that currently apply to funds to model portfolios or requiring firms to use standard terminology to describe their strategy and asset allocation.

Addressing potential non-compliance with our rules

1.49 Some platforms supply services paid for by consumers which might alter an adviser's incentives, without considering whether the provision or receipt of the service might constitute a non-monetary benefit which needs to comply with our inducement rules. Both financial advisers and platforms should consider whether the non-monetary benefits that they receive or offer comply with the FCA's inducement rules.[12]

1.50 Investment platforms providing stockbroking services to retail investors can do more to consistently achieve and demonstrate the best execution results for their customers. We currently consider our rules are sufficient. Firms complying with our rules should provide retail investors with the information they need about how their orders will be executed by the firm. However, we welcome feedback on whether retail investors would benefit from greater transparency.

Next steps

1.51 We are publishing this interim report to give all interested parties an opportunity to comment on our emerging thinking and analysis. We invite comments on:

- our interim findings on how competition works between investment platforms
- our potential remedies and, specifically, the questions set out above and in Chapter 9

1.52 If you have comments on the questions then please send your comments to investmentplatformsmarketstudy@fca.org.uk by 21 September 2018. Please provide reasons and evidence in support of your views. We will analyse your feedback, and any further information we receive in the course of our ongoing engagement with the sector, and publish our final report in the first quarter of 2019.

12 For example, COBS 2.3 (for non-MiFID business) and COBS 2.3A (for MiFID business) contain rules which govern the circumstances in which a firm might be able to pay or receive a non-monetary benefit.

2 Introduction

Investment platforms are growing and are being used by an increasing number of retail investors. We launched the Investment Platforms Market Study because we wanted to assess whether these investors and their financial advisers can make informed choices between platforms, informed choices between products on the platform and whether platforms help consumers get a better deal by placing pressure on asset managers to offer competitive products on platforms.

We are publishing an interim report to set out our interim findings, provisional remedies and next steps.

We are inviting feedback on our provisional findings and remedies. Please respond to investmentplatformsmarketstudy@fca.org.uk by 21 September 2018 if you have comments on our interim report. We will assess feedback from stakeholders and publish our final report in the first quarter of 2019.

The key features of the platform market

2.1 In broad terms, we define a "platform service" as a service which offers access to third party investment products.[13] Platforms allow investors and financial advisers to buy, sell, hold and manage investments. For more information about the investment platform sector and its participants please see Annex 1.

2.2 There have been investment platforms in the UK for almost 20 years, but they have grown significantly in the last 10. The platform market has doubled since 2013 from £250bn in assets under administration ('AUA') to £500bn.[14] The increase is the result of both the growth in value of the assets held on platforms and of the inflow of new assets.

2.3 Platform users are on average older and wealthier than the general population, although there are significant differences between platform users such as their motivations and confidence when investing.

2.4 Platforms differentiate themselves through the depth and breadth of the products and services they offer. Some offer services specifically tailored to advisers (adviser platforms), others to the end customer D2C. Platforms can be stand-alone or part of a broader financial services offer.

2.5 Changes in individual market shares have been limited since 2013, but smaller firms have been gaining market share. The overall market has become less concentrated.

13 See https://www.handbook.fca.org.uk/handbook/glossary/?filter-title=platform+service. So far as is relevant to the present context, the Handbook definition of a platform service is a service which: (a) involves the arranging and safeguarding and administering investments; and (b) distributes retail investment products which are offered to retail clients by more than 1 product provider.

14 Total AUA figures are taken from data submitted by platform service providers to our request for information. The data covers retail customers (including advised and non-advised) and are year-end AUA from 2013 to 2016 and the AUA at the end of June 2017. 1 large platform was excluded from our data request so the figures may underestimate the total size of the market.

Three investment platforms have entered the market during the last 5 years. However, the AUA of new entrants represents a negligible fraction of the market.

The scope of the study

2.6 Platforms are part of a wider value chain including wealth managers, insurance firms, banks and asset managers with a direct route to market. Some of these firms offer similar services as they provide consumer access to retail investment products through an online portal.

2.7 Our analysis has covered:

- platforms and other firms that offer online access to retail investment products[15]
- retail investors who access retail investment products online
- intermediaries, including financial advisers and wealth managers who use platforms to access different retail investment providers on behalf of their clients
- product and wrapper providers who use platforms to distribute their products
- technology providers to whom platforms outsource services
- fund ratings and data providers whose information platforms use and distribute

Market features explored through the study

2.8 Through the market study we have explored 7 key features of the investment platforms market in order to understand whether competition between investment platforms is working in the interests of consumers. We have explored:

2.9 **Consumers' use of platforms:**[16] We outline our findings into consumer preferences, behaviour and whether consumers can make informed choices in Chapters 3 and 4 and Annex 2. In Chapter 3 we outline our findings into how consumers choose, use and switch platforms including the barriers to switching without the help of a financial adviser. In Chapter 5 we outline our assessment of whether consumers are able to access transparent and useful information to help them choose between platforms and investment products on the platform.

2.10 **Advisers' use of adviser platforms:** We outline our findings into the impact financial advisers have on competition between advised investment platforms in Chapter 4. We explore what factors advisers prioritise when choosing, reviewing and deciding whether to switch platform, the reasons why and whether platforms consider the end investor when competing to win business from advisers.

15 Other distributors could include financial advisers, wealth managers, discretionary investment managers, life companies and banks who provide retail investors services which are similar to that offered by a platform, but without necessarily providing access to third party investment products.

16 Through the report consumers refers to retail investors.

2.11 **How platforms influence consumers' investment choices:** Some consumers use their platform to choose between a wide range of investments while others depend on their platform to guide them how and where to invest. For consumers who use their platform to help them choose between investments it is important that consumers can make informed choices free of product bias. In Chapter 6 we explore whether platforms enable them to do so.

2.12 **What impact platforms have on fund charges:** In Chapter 6 we explore whether firms have the incentive and ability to negotiate fund charges and what the implications are for a platform's ability to compete on a total-cost basis by reducing fund charges.

2.13 **Whether platforms have processes in place to ensure Best Execution:** Platforms account for a large share of the UK retail stockbroking market. In response to feedback we received on our Terms of Reference, we assessed how platforms approach their stockbroking services and whether their approach is likely to deliver value to consumers who use platforms to invest directly in securities. We outline our findings in Chapter 6.

2.14 **Competitive outcomes:** We examined whether consumers' choices of platforms and what those platforms offer in terms of price and non-price features are consistent with effective competition. We explored whether consumers appear to be making good choices and are getting value for money given their preferences and how platforms differ. We outline our findings in Chapter 7.

2.15 **Barriers to entry and expansion:** We wanted to understand whether there are barriers to entry and expansion in the sector which might be preventing platforms competing on the price, quality and value for money of their offering. Our analysis of barriers to entry and expansion is informed by our analysis of platforms' business models and profitability. We outline our findings on barriers to entry and expansion in Chapter 8.

What evidence did we gather to support our analysis?

2.16 Our interim findings are drawn from multiple pieces of analysis including:

- Consumer research including 48 interviews and an online survey of over 3000 platform consumers to understand the investment journey for advised and non-advised investors. The findings from our consumer research are set out in Annex 2 and further information about the methodology can be found in Annex 3.
- Quantitative analysis of consumer preferences and choices (see Annex 8).
- Financial analysis which assessed how platforms generate revenues, the relationship between platform costs, key firm characteristics and platforms' operating margins. Further details of our approach and findings can be found in Annex 4.
- Econometric analysis of what determines the size of fund discounts (see Annex 7).
- Quantitative and qualitative analysis of 40 platform and 21 comparable firm responses to our information request. We used the responses to assess a range of market features including the services offered by platforms, prices, market shares and entry/exit.

- Analysis of 166 financial advice firm responses to an information request.

2.17 In addition, we met with a wide range of over 50 stakeholders through the study including platforms, comparable firms, technology providers and industry groups.

3 How do consumers choose, use and switch platforms?

In this chapter we provide an overview of the needs and preferences of consumers, and their role in driving competition in the market.

We find platform consumers have significantly different characteristics and motivations for using platforms to invest. Most consumers value the control, access and convenience of platforms. Many are very knowledgeable about finance and use platforms for a range of their investments. Others are less confident investors or prefer to use an adviser who then invests through a platform. Multi-homing, where consumers use more than 1 platform is fairly common – 37% of all consumers in our sample.

When choosing a platform, nearly half (44%) of consumers who do not have an adviser ('non-advised consumers') have researched more than 1 platform. However, most non-advised consumers either have not shopped around, cannot remember whether they did, or were moved onto the platform without making an active choice.

Most non-advised consumers are satisfied with the activities they undertake on platforms and how platforms deliver the various features they value. The main source of dissatisfaction appears to be charges.

While charges are an important factor to non-advised consumers, other factors are also important. These include having a range of available investment products, the look and feel of the platform, and the tools and support they provide. Despite consumers stating that charges are important, their awareness of platform charges is fairly low. 29% of consumers either do not know whether they pay charges for investing via a platform or think they do not pay any. Consumers also make significant errors estimating how much they pay in platform charges.

Overall, our consumer research shows that switching levels are low. A small number of consumers (just over 3% a year on average) have switched directly without help from an adviser in the last 3 years. Around 6% of consumers a year have added another platform rather than switched fully. 7% of consumers have tried to switch 'directly' at some point but have failed to do so.

We found significant barriers to switching. Both firms and consumers say the time involved, complexity and exit fees create barriers to switching. Data from firms suggests that switching times vary depending on what investments and wrappers the consumer is switching and the process. Generally, switching takes from a few weeks to a few months.

Introduction

3.1 Engaged and active consumers can drive effective competition in the platforms market. They can do this by shopping around, comparing platform features, monitoring the ongoing competitiveness of their platforms and switching platforms if they find a better deal.

3.2 This chapter presents our findings on consumer behaviour, preferences and experiences in this market:

- we first provide an overview of the consumer journey, focusing on how non-advised consumers choose and use platforms
- we then analyse consumer preferences in more detail
- finally, we examine switching behaviours and barriers to switching

3.3 Much of the analysis in this chapter is taken from consumer research we commissioned from NMG Consulting[17] (NMG), based on data firms provided to us during the course of this study.[18] We also carried out further analysis combining the anonymised consumer research data with the data from platforms.

3.4 Unless stated otherwise, our definition of 'advised' and 'non-advised' consumers refers to the status of the consumer on the sample platform, ie the specific platform that the survey asked about.

3.5 This chapter focuses on the non-advised consumer 'journey' (the stages consumers go through when making choices) but we also consider consumer behaviours and preferences more widely. Chapter 4 focuses on advised consumers and the role and behaviours of advisers for investments using platforms.[19]

The non-advised consumer journey

3.6 Here we explore key stages of the consumer journey and profiles of platform users, focusing on non-advised consumers.

Reasons for using a platform

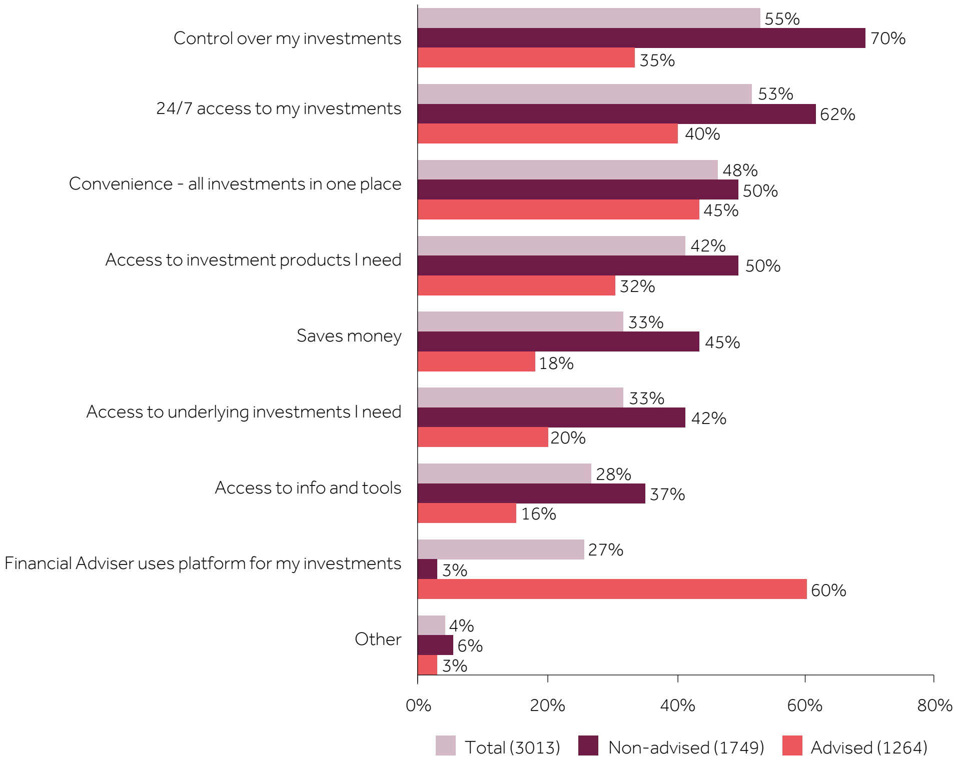
3.7 Figure 3.1 below shows that the 3 main reasons non-advised consumers give for using a platform are control, access and convenience. These findings are consistent with our qualitative research.

17 See NMG's full report at Annex 2 and Technical Report at Annex 3. In this chapter, all graphs include the relevant questions numbers as asked in the consumer research for reference.

18 Given the target population of platform users is a small and atypical fraction of the overall UK population, and the practical difficulty of carrying out consumer research on such a population, our research was greatly enhanced by platforms' ability to provide the necessary data to carry out the consumer research.

19 Information provided by firms in response to our information request included copies of consumer research they have undertaken. Our review of firms' own consumer research identified common findings to our research including: varying motivations, needs and behaviours of different consumer segments, the prevalence of multi-homing, importance and value of information, tools and calculators provided by platforms, low awareness of charges, mixed use and views of filtered fund lists and model-portfolios, the importance of brand and barriers to switching.

Figure 3.1: Main reasons for using an online investment platform



Base: All respondents (see chart)
S2Q1 What are your main reasons for using online investment platform?

How do consumers choose their platform?

3.8 The ability of consumers to identify and select their preferred platform is one of the main drivers of competition. In this section we explore evidence on how consumers shop around and choose platforms, focusing on non-advised consumers. Advised consumers typically have little or no involvement in choosing platforms (see Chapter 4). Chapter 5 examines this further by assessing whether consumers have the information to shop around and choose effectively.

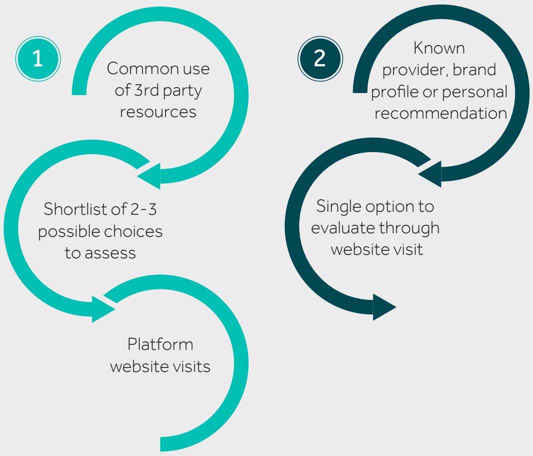
3.9 Overall, fewer than half (44%) of all non-advised consumers research multiple platforms, compared to 18% who research only 1 choice and 10% who carry out no research at all. A relatively large minority of non-advised consumers (16%) say they have been moved to a platform and so played no role in researching platforms.[20]

3.10 Our qualitative research suggested that while many non-advised consumers actively choose their platforms, this is often a second decision, as the choice of platform may be firstly driven by the choice of investment product they are seeking. This is supported by evidence in Figure 3.1 which highlights that over a quarter of non-advised consumers said access to specific investments was important when choosing a platform, and that availability of investment choices was among the most important factors.

3.11 Where consumers researched multiple platforms, over half use the information on the platform and just under half are using other online sources (financial magazines, newspapers) to do so.[21]

20 See Figure 14 in NMG report at Annex 2.
21 See Figure 16 in NMG report at Annex 2.

Figure 3.2: Non-advised consumer journeys when shopping around for a platform



Our qualitative research identified two main research journeys by non-advised consumers when choosing the platform:

Journey 1 - consumers use independent sources to create a shortlist that they feel is appropriate to their needs. These consumers use the platform's website to explore the brand, experiment with the look and feel of the website and will often look at charges.

Journey 2 - consumers are driven by behavioural shortcuts and only research one platform, or carry out no research at all. These shortcuts include recommendations from family and friends, a preferred brand or perceived reputation and are often used in combination.

> ***I have gone with xxx because they have a first-class reputation [and] on family recommendation therefore I feel it is trusted and they have a fantastic app.'*** ***Non-advised consumer***

3.12 Our research asked non-advised consumers what factors determined which platform they chose. We found platform choice was driven equally by the breadth of investment choices and platform charges (see Figure 3.5). The range of products, the look and feel of the platform, telephone and online support are important, too. We consider these factors further when we assess consumer preferences in paragraphs 3.31 to 3.43 below.

3.13 Our consumer research also found that multi-homing is fairly common, with 39% of non-advised consumers investing through 2 or more platforms.[22] On average, the non-advised multi-homers are an older and wealthier[23] sub-group of platform consumers, with greater self-stated levels of awareness and financial knowledge. They tend to report having done more shopping around for platforms than non-advised consumers who use only 1 platform. However, they do not seem to have researched charges more or be more aware about platform charges than the single-homers.

3.14 The main reason given for multi-homing was to diversify risk.[24] As diversifying investments on the same platform can also diversify risk, we explored this further through our qualitative research (see box below).

3.15 Multi-homing can be important in helping apply competitive pressure to platforms. Through multi-homing, consumers may learn about alternative offerings which enables them to shop around and choose platforms in a more informed way. While a relatively high proportion of consumers multi-home, not all the reasons they gave for doing so are likely to mean they are more informed or active. Examples include when a range of people are involved in choosing different platforms or when multi-homing

22 See Figure 9 in NMG report at Annex 2. This finding is consistent with firms' own consumer research, though levels of multi-homing can vary across platforms.
23 Based on total investable assets.
24 See Figure 13 in NMG report at Annex 2.

is the result of workplace pension arrangements. There may also be less impact from consumers who multi-home on adviser and D2C platforms (ie who multi-channel) as in practice there may be little read-across between the 2 channels; these consumers represent 14% of the total (37% of the multi-homers).

Financial Services Compensation Scheme (FSCS) levels of protection

In our qualitative research we found that diversification is partly driven by concerns over financial security. Consumers want to keep their invested money safe and considered dividing assets across platforms as the best way to achieve this. As one consumer told us:

"One of the reasons I split the money is that I am concerned about how secure the money is if you put all your money in one place you could lose that money so spreading it around gives you some guarantee." ***Non-advised consumer***

We also heard some misconceptions about the custodial role of platforms, as well as confusion about the FSCS protection limits for investments. This issue was also identified in research provided by 2 firms as part of this study.

This can be a complex area for consumers, particularly where third parties are involved and different levels of protection may apply. We found that platforms may not be doing enough to ensure that all disclosures are clear, accurate and not misleading for their specific firm.

As well as this Market Study, we have been reviewing the funding of the FSCS (Consultation Paper CP17/36). On 1 May 2018 we published our feedback and finalised rules to that consultation Paper (CP18/11). These confirmed an increase in the FSCS compensation limit for investment provision and investment intermediation claims from £50,000 to £85,000. These changes will come into effect from 1 April 2019 and will remove some of the differences in the limits on FSCS compensation from that date.

How do consumers use their platform?

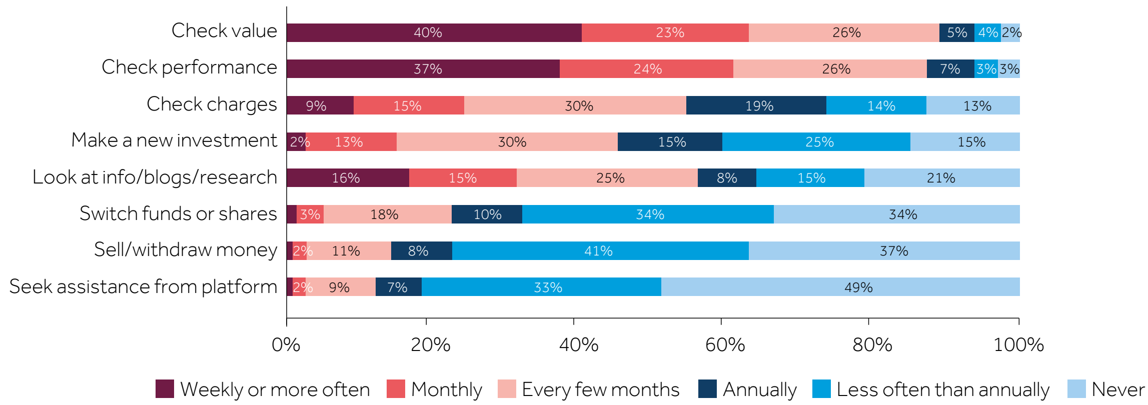
3.16 Our consumer research and firm response analysis explored the ways non-advised consumers use platforms for selecting, monitoring and switching their investments, and consumer satisfaction.

Activities carried out on platform

3.17 Figure 3.3 shows some significant differences among non-advised consumers in how they use the resources platforms offer and how often they carry out activities on platforms. Almost all non-advised consumers equally report checking the value and performance as the most common activities undertaken, but they check charges much less frequently.

3.18 Non-advised consumers seem to use platform information resources to a relatively limited extent. 79% of consumers look at the information, blogs and research the platform provides but most only do so every few months or less, and a significant proportion do so less frequently than once a year. We can also see that nearly half (49%) of non-advised consumers never seek assistance from platforms.

Figure 3.3: Activity frequency for non-advised respondents



Base: Non-advised respondents (1749)
S5DGQ5 How often (if at all) do you understand each of the following activities on (platform)?

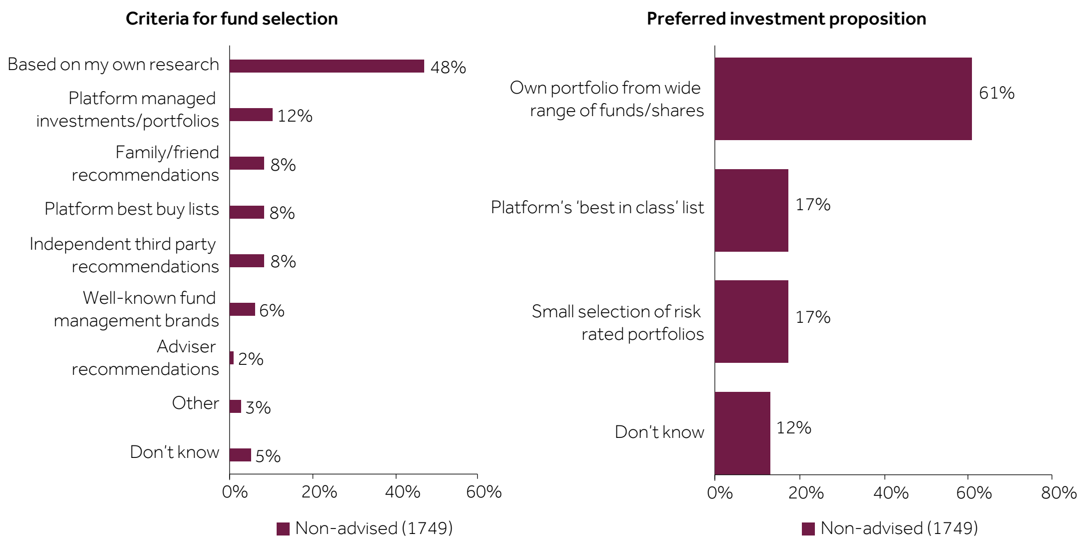
3.19 Our qualitative research identified some examples of respondents using platform tools, though many of the more active and informed consumers in the qualitative research largely use third party sources of information.

Selection of investment products

3.20 We observed 3 general approaches to how non-advised consumers choose investments on platforms: 'Do it myself', 'Do it with me', 'Do it for me'. These are consistent with the way some platforms identify how consumers make decisions and how they rely on platforms to help them make investment decisions.

3.21 As Figure 3.4 shows, once on a platform, over half (61%) of consumers prefer to build their own portfolio from a wide range of funds/shares. When selecting a specific fund, nearly half of consumers select funds based on their own research, compared to just 12% who select based on platform managed investments and portfolios. This indicates the majority of non-advised consumers prefer to 'do it myself'.

Figure 3.4: Choosing Investments



Base: Non-advised respondents (see chart)
S3DG16 Thinking about how you chose to invest on the [platform] platform, which of the following best describes your choices?
S3DGQ21 Thinking about choosing your investments on the [platform] platform, did you:

3.22 On average in the non-advised sample, 17% use a platform's 'best in class' fund lists and 17% use pre-set risk-rated portfolios as shortcuts to help their decision making.[25] We carry out further assessment of best buy lists and model portfolios in Chapter 6.

3.23 Our qualitative research found that for less-experienced consumers or those new to investing select lists and/or model portfolios appear to provide a useful shortcut in making decisions when choosing from a full range of funds.

> ***"There were 3 different arrangements, high, medium and low risk and I chose the middle one… it was xxx pre-packaged, easy investment management as not having to make many decisions'***
>
> ***Non-advised consumer***

3.24 Our qualitative research found more experienced consumers were sceptical about platforms' objectivity when designing and formulating these lists. While these consumers may use select lists and/or model these to help supplement or validate their own research, they are not the main driver of their decisions. These consumers prefer instead to do their own research of independent sources.

> ***"I am always sceptical of top 150 or equivalent from other platforms because there is always going to be some bias. I would rather go to someone who is producing independent information'***
>
> ***Non-advised consumer***

25 See Figure 24 in NMG report at Annex 2. When we included only platforms that offer model portfolios and/or best buy lists in the analysis, we found similar reported levels for consumers using model portfolios and/or best buy list (20% and 17% respectively). However, our analysis also found that some consumers had cited the use of these features despite the fact they are not available on their platform. This suggests a potential lack of understanding about what was meant by model portfolios and best buy lists.

Consumer experiences and satisfaction when using a platform

3.25 Our qualitative research found that consumers consider a platform's value for money is a combination of charges, platform non-price features, and investment performance. However, particularly for charges, consumers perceived there to be a 'much of a muchness' across the market.

> *I think it can be cheaper, it can always be cheaper but…it's based on customer experience, user experience, I should have the information available any second doesn't matter where I am or what I'm doing'*
>
> ***Non-advised consumer***

3.26 Our consumer survey found that the majority of non-advised consumers are very or quite satisfied with the delivery of factors that are most important to them. Charges attract the highest levels of dissatisfaction, with 14% of respondents stating they are dissatisfied.[26]

3.27 However, our qualitative research also found that consumer satisfaction levels are sometimes linked to satisfaction with overall investment returns, which tend to be attributed to the performance of the platform. This suggests some confusion about consumers' understanding about platforms' administrative function as opposed to the performance of investment products. So it is possible that consumers' relatively high satisfaction levels with platforms could be influenced by the positive performance of financial markets in recent years.

Conclusions on the consumer journey

3.28 In summary, we see that a significant proportion of non-advised consumers shop around and research more than 1 platform. However, the majority of non-advised consumers have not shopped around when choosing a platform, or cannot remember whether they looked at other platforms before making a choice.

3.29 We find that, as with choosing the platform, consumers report charges being one of the most important features, alongside a range of non-price features such as breadth and range of investment choices and products, the platform's look and feel, brand and support.

How important are platforms' price and non-price features for consumers?

3.30 Here we bring together evidence to help us understand consumer preferences for platforms' price and non-price features. As we have found that consumers consider platform charges important when choosing a platform, we also consider how aware they are about the charges they incur or might incur when using a platform.

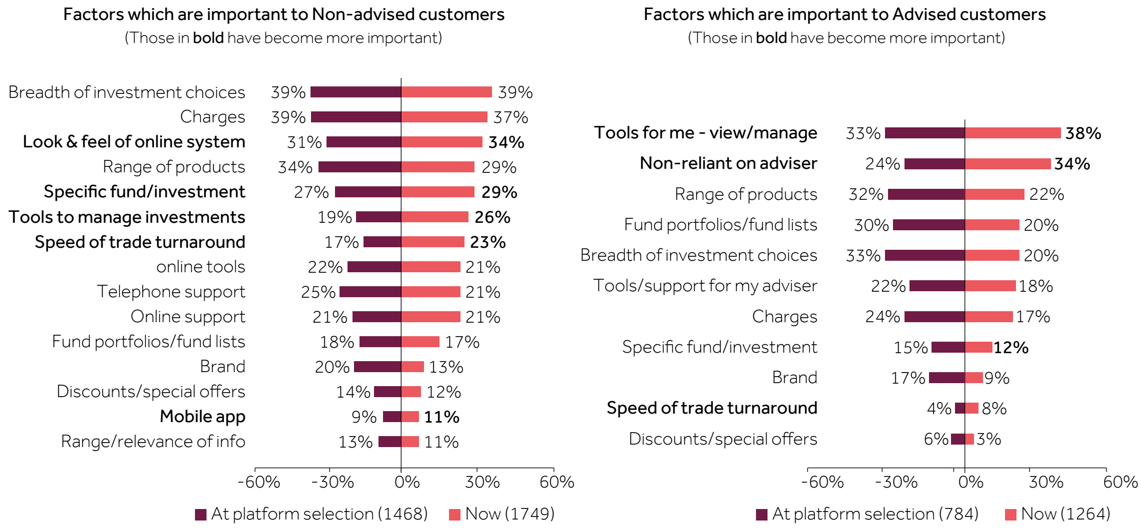
Consumer preferences

3.31 Our consumer research asked consumers what factors determined their choice of platform. For non-advised consumers, we found that the breadth of investment choices and platform charges are the 2 most important factors when choosing a

26 See Figure 47 in NMG report at Annex 2.

platform. As shown in Figure 3.5 below, other important factors are range of products, the look and feel of the system, telephone and online support. For the advised consumers, tools to manage and view the investments and the breadth of investment choices are the 2 most important factors, with charges being relatively less important.

Figure 3.5: Important factors in platform selection vs importance in current usage of platform



Base: 'Now'; All respondents, 'At platform seletion'; Non-advised respondents excluding those moved onto the platform/Advised respondents with some involvement in decision (see chart)
S3DGQ6/S3AGQ3 From the list below which features most influenced your decision to invest through the [platform] platform?
S5DGQ1/S5AGQ1 Which of the following features are most improtant to you now, based on the way you use the [platform] platform?

3.32 The evidence from the survey is supported by findings from our conjoint analysis.[27] Our conjoint analysis asked consumers to choose between platforms with 6 different attributes: brand, range of investment options available (including model portfolios), ease of use, reporting features, research features, and price.[28]

3.33 We found that price is the most important factor for consumers, though there are significant differences in preferences amongst different consumers (see Figure 3.6 below):

- Price (27%[29]) is on average the most important attribute for consumers, but they also rank brand (23%) and range of investment options (18%) highly. Collectively, non-price factors add up to 73%, which suggests that consumers value these attributes.

- Each of the 6 factors was the most highly valued attribute for at least some respondents in the sample. The majority of consumers (60%) said non-price attributes were the most important, with brand (32%) scoring particularly highly. However, low price was the most important attribute with 40% of respondents choosing it as the most important attribute in their choice of platform.

27 Further details about the design and implementation of the conjoint are available in the NMG report in Annexes 2 and 3. Our own analysis of conjoint data is detailed in Annex 8. The analysis of consumer preferences and price sensitivity set out in this chapter includes both advised and non-advised consumers.

28 These attributes were identified after preliminary research, including in-depth qualitative interviews with consumers. To note that in the context of the conjoint analysis, 'price' refers to platform headline charge.

29 Percentages provide a measure of the relative importance of each attribute to consumers. Technically they estimate the difference each attribute could make to the total utility of a product.

Figure 3.6: Conjoint analysis: implied preferences for price and non-price attributes

	Brand	Range of investment options	Ease of use	Reporting	Research	Price
Overall importance of attributes	23%	18%	10%	10%	13%	27%
Most important attributes	32%	18%	5%	2%	3%	40%

3.34 Consumers' preferences also depend on their personal characteristics, such as financial confidence, engagement, and attitude to risk, personal wealth, and whether and how they choose to use a financial adviser. We found that consumers that are less knowledgeable and less confident about managing their investments place a higher value on brands and on platforms that are easier to use, whereas more knowledgeable consumers place considerably higher value on the range of investment options offered. The importance of the range of investment options available also increases with the wealth of the consumer.

3.35 Preferences also vary with whether consumers have a financial adviser and, for those that do, how they choose to use them. Those consumers who rely most on their financial adviser for decision making have, on average, a higher preference for brand and are less price sensitive[30] than other consumers. Those who do not have an adviser, or who have an adviser but take decisions largely independently from them are on average more price sensitive and place a greater value on the range of investment options available.

3.36 The evidence from our conjoint analysis suggests that consumers typically place a high value on brands. For example, on average consumers are willing to pay between 17 and 19 basis points (bps) for a well-known financial institution or a platform specialist. There is considerable variation in these valuations with 25% of our sample valuing brand at 32 basis points (bps) or more.

3.37 While consumers also value the range of investment options attribute, there are a range of consumer views. Some prefer a more restricted choice and model portfolios, although most prefer a much wider range of choice of investment options. On average consumers are prepared to pay between 9bps and 17bps for this attribute.

3.38 Although brand and the range of investment options are the 2 highest valued non-price attributes, consumers appear willing to pay for other non-price attributes too. The conjoint analysis estimates that these other non-price attributes (ease of use, reporting and research) are on average valued at between 6bps and 9bps.

3.39 Our qualitative research also found that consumers are happy to pay a price for the services they receive from their platform; illustrating that quality of non-price features are important for some consumers.

30 In the context of the conjoint analysis we use the term "price sensitive" to refer to consumers who place a high valuation on low platforms prices (relative to other consumers). Similarly, "non-price sensitive" consumers are those that place a relatively low valuation on low platform prices.

> ***"As long as I am not being radically overcharged I don't mind paying if [the service] is good'***
>
> ***Non-advised consumer***

Consumer price sensitivity

3.40 We considered how responsive consumers are to platform charges and found that the evidence on price sensitivity is mixed.

3.41 The conjoint analysis shows that consumers do value non-price attributes of platforms, particularly brand and portfolio choice, but price is the most important attribute for most consumers. It is also the most important attribute overall. We explored which types of consumer are the most and least price sensitive. We did not find that any particular group of consumers is significantly less price sensitive than others (see further details of this analysis in Annex 8).

3.42 On the other hand, our analysis of aggregate flows into and out of platforms following a price change indicates consumers are not responsive to these price changes. We examined how consumers have reacted to changes in platform charges between January 2014 and June 2017. If consumers were price sensitive, we would expect to see increased flows into a platform after it has reduced platform charges, and money leaving the platform when charges increase. We analysed flows (inflows and net flows) following any changes to each of the main charges separately across 24 D2C platforms. We also compared the flows of platforms with price changes to the flows of platforms without any price changes.

3.43 We found that when platforms increased or decreased any of their main charges[31] it had no significant impact on flows in and out of the platform. Our only consistent finding is that platforms, regardless of a price change or not, usually experience a growth in fund inflow during the end of the ISA period.

Awareness of charges

3.44 We found that consumers research and understand platform charges[32] to a much more limited extent than their stated importance of charges implies. Our consumer research also found that 43% of non-advised consumers say that they researched charges when choosing a platform, with a further 14% saying they researched charges but it was difficult to find the information. However, a quarter (25%) said they did not do any research into charges and 16% said they don't remember whether they researched charges.[33]

3.45 Figure 3.7 shows that nearly a third (29%) of all consumers do not think that they pay platform charges (10%) or do not know whether they pay platform charges for investing (19%). This is broadly similar for advised and non-advised consumers.[34] These findings are supported by the qualitative research where a significant proportion was unsure if they were paying an ongoing platform charge.

---

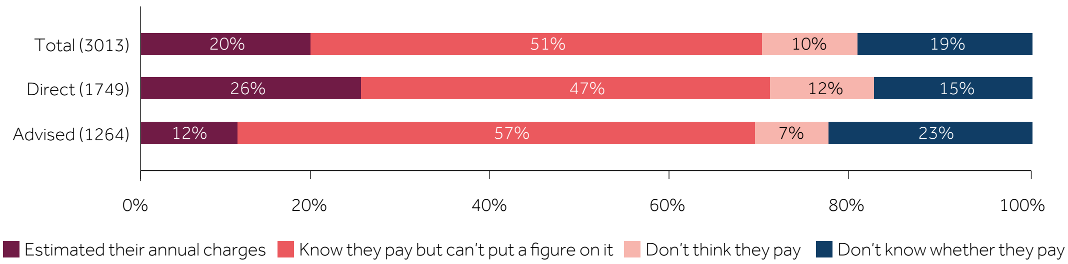
31 By main charges, we considered headline platform fee, dealing charge, ISA fee, SIPP fee, GIA fee, set-up fee, exit fee and cash interest.

32 In the consumer research our questions focused on the total platform charges however it is possible that consumers interpreted these questions more broadly to include other charges, or more narrowly just including platform fee/headline charge.

33 See Figure 36 in NMG report at Annex 2.

34 Please see Chapter 4 for further analysis of advised consumers.

Figure 3.7: Awareness and estimation of platform charges



Note: All respondents (see chart) S3DGQ9a/S3AGQ4a Do you pay any charges for investing through the platform? S3DGQ12b/S3AGQ6b How much, approximately in pounds, have you paid in platform charges over the last year (12months)

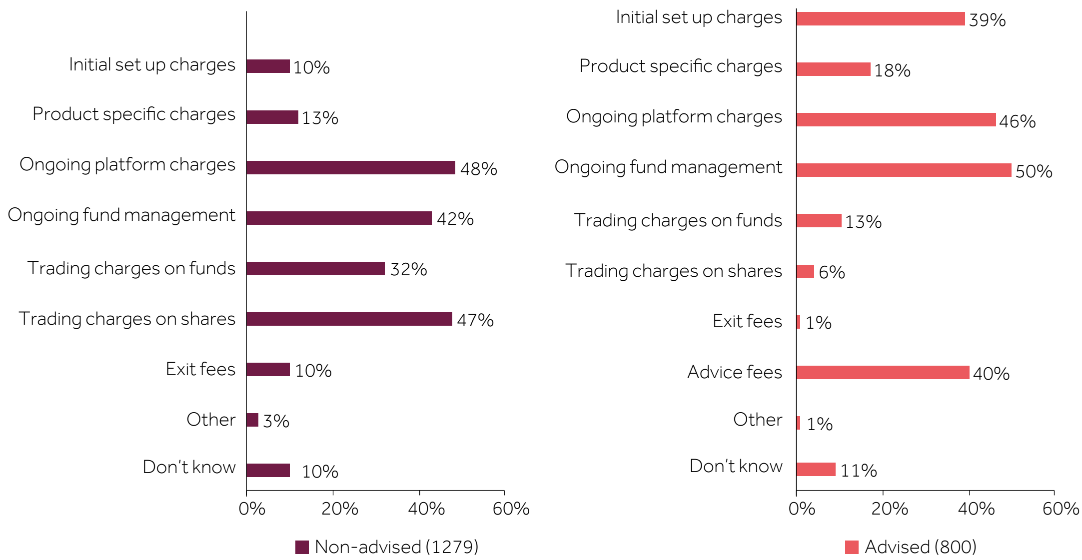
3.46 26% of the non-advised consumers attempted to estimate their annual platform charges when asked to do so, compared to only 12% of advised consumers and 20% overall. However, the estimates provided were generally inaccurate. We compared consumers' responses to firm data of actual charges paid. We found that 60% of consumers incorrectly estimated their platform charges by at least 50%.[35]

3.47 As shown earlier in Figure 3.3 the consumer survey found that most consumers rarely check the charges they pay. 14% of non-advised consumers state that they check charges less than annually and 13% never. Only 20% of all consumers attempted to estimate annual platform charges when asked, which suggests that the number of consumers who check charges may be significantly lower than stated. It also suggests that when checking charges, consumers are unable to either access or understand charges being applied or calculate a total annual charge.

3.48 Figure 3.8 below shows that consumers have a mixed level of awareness of other charges that they thought applied when they chose to invest via their platform. While some of these charges may not have applied to every consumer depending on their specific investment and platform, we see low awareness of product specific charges and exit fees. 10% of consumers also did not know what charges applied. This suggests that consumers are unlikely to be able to estimate the total cost of investing through a platform or consider it when choosing and using the platform.

35 This included both under– and over-estimating of actual charges paid, with over-estimation being more common.

Figure 3.8: Charge types believed to apply at the time the platform was chosen



Base: Those who are aware they pay charges (see chart)
S3DGQ11/S3AGQ5 Which, if any of the following charges applied at the time you chose to invest through the [platform] platform?

3.49 Of those who thought these charges applied, some non-advised consumers found it quite or very difficult to understand the information about each of these charges. Exit fees were most commonly cited as quite or very difficult to understand (26% of consumers); [36] but product specific charges and ongoing management fees were also quite or very difficult to understand (15% and 14% of consumers respectively).[37] The difficulty consumers have in understanding the charges may explain our qualitative research finding that consumers struggle to separate out the various charges within the total cost of investing such as platform charges, specific product and wrapper charges and fund management charges.

3.50 The qualitative research suggested several reasons why consumers are not engaged with or know about platform charges. These include charging structures that vary across the market, platform charges being considered of lower importance compared to other charges and the assumption that the platform charge is a very low percentage with charges being 'much of a muchness' across the market. We heard that consumers are content with current levels of charging, despite them not being able to say what charges they paid, so long as they did not think these were excessive and they still achieved a net return overall. See Chapter 5 for further analysis on the complexity of charges.

Conclusions on the importance of price and non-price features

3.51 The evidence on consumer preferences we gathered through our consumer research suggests that platform charges are important for a significant proportion of consumers. But it also suggests that non-price features are very important, too, and can drive consumers' choice of platform. Some value price more than non-price features, while for others it is non-price features such as investment choices, brand, look and feel of the platform or customer support that are more important than price. These findings form the basis for our assessment of whether platforms appear to compete in the interests of consumers and of consumer outcomes in Chapter 7.

36 Please see further detail on exit fees in paragraph 3.68.
37 FCA analysis based on NMG survey data.

3.52 In terms of price, we found that, while consumers state in the survey that it is important, over a quarter (29%) do not know whether they pay platform charges or what they pay, and the majority cannot estimate the charges. Even when consumers attempt to estimate the platform charges they pay, most make errors. This is despite over half of consumers reporting checking charges at least every few months.

Are there barriers to switching platforms?

3.53 Consumers' ability to identify and select their preferred platform is the main driver of competition. A consumer's decision to move to another platform that better meets their needs and preferences in terms of price, choice of investments or products, or other features is a key component of this process. So barriers on consumers' ability to switch may mean platforms face weak competitive pressure.

3.54 For this reason, and focusing on switching directly without the help of a financial adviser (switching adviser platforms is discussed in Chapter 4), we sought to understand:

- the nature and process of switching in the platforms market
- what drives switching and what consumer characteristics are associated with switching
- whether the observed switching leads to better outcomes for those who switch and whether it stimulates competition
- any barriers to switching

What are the levels of switching in the platforms market?

3.55 Given the nature of the service platforms provide, 'switching' in this market can occur in a number of ways. The switching might:

- involve existing assets, new assets, or both
- involve moving all assets or just a part of them
- be sudden or gradual (eg include an initial phase of 'testing the waters')

3.56 Consumers multi-home in this market and multi-homing can sometimes be a step in the process of switching, or encourage future switching. Consumers can also decide to withdraw their assets and invest them somewhere else that is not on a platform, for example with a fund manager or pension provider. When switching, consumers can act on their own (self-directed) or be assisted by an adviser.

3.57 The process of moving assets to a new platform may take different forms, mainly:

- cashing-out then buying the same, or different investment products elsewhere
- opting for a re-registration transfer, where the new platform simply re-registers the asset rather than the consumer having to sell and then re-buy it

3.58 Different processes have different characteristics and implications. For instance, cashing-out may imply an obligation to pay taxes, whereas re-registration transfers can take a long time to be completed.

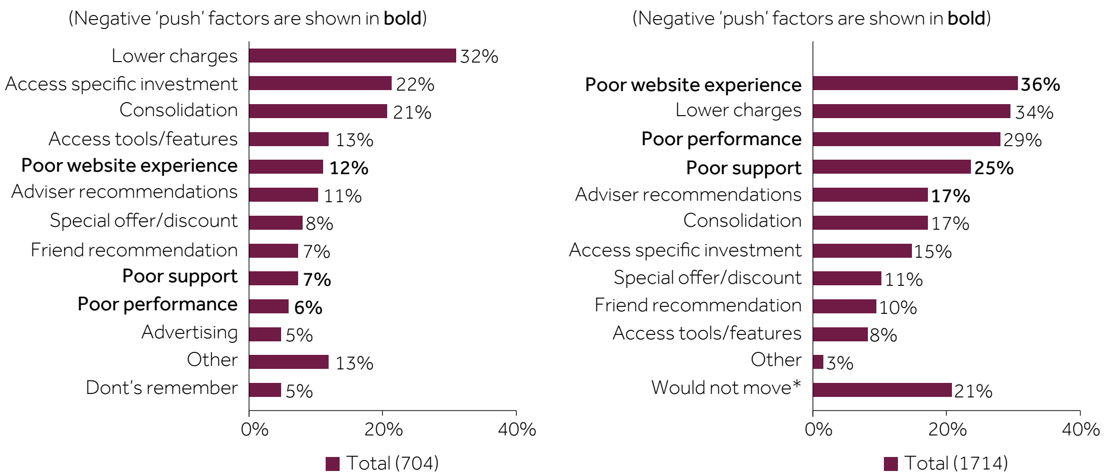
3.59 Our consumer survey asked consumers about 'direct'[38] switching they had undertaken in the previous 3 years. Only 10% of consumers have switched in the last 3 years, equating to an average annual switching rate of just over 3%. Around 6% of consumers a year have added another platform rather than switched fully.[39]

3.60 Multi-homing and switching are closely related. 49% of multi-homers have switched or started using an additional platform in the last 3 years compared to 14% of consumers who only invest through 1 platform.

What are the drivers for switching, and who are the switchers?

3.61 Our consumer research asked the reasons why consumers have switched[40] and, for those who have not switched, why not and potential reasons for doing so in the future. Our survey suggested that nearly half (46%) of those who have not switched nor considered switching are happy as they are.[41] We found that switching behaviour can be triggered by a number of push and pull factors. As Figure 3.9 shows, push factors can be based on negative experiences on the existing platform compared to the pull factors of a more appealing offer by another provider, access to specific funds and consolidation of assets.

Figure 3.9: Actual and potential reasons for switching platform



'Other' includes: New workplace pension, Risk diversification, Pushed by provider (eg ceased trading)

Base: Those switching one platform to another or adding an additional platform (see chart)
S6bQ5 Thinking about the most recent time you moved from one platform to another, what were the main reasons you wanted to move?
*Note: all switching activities include the possibility that some existing investment is left on the platform

Base: Those who have not switched nor considered switching but would not leave it to their adviser either (see chart)

S6bQ16 Which, if any, of the following reasons would prompt you to move your investments away from a platform (without the help of a financial advise)?
*/wouldn't move without help from a financial adviser

Note: excludes those who have moved off platform or switched to advised

38 Defined as moved to another platform all or most of investment. See Figure 41 in NMG report at Annex 2.

39 Thus, a larger proportion – 27% in the last 3 years or 9% per annum on average – have 'switched' in a broader sense, including moving investments from one platform to another but also added additional platforms whilst continuing to use the current platform. See NMG report Annex 2 for further analysis.

40 Here we consider switching in a broader sense, ie switching platforms fully as well as adding additional platforms and moving investments off platform. See Annex 2 for further details.

41 See Figure 46 in NMG report at Annex 2.

3.62 Our consumer research found that the key driver for switching platforms is access to lower charges,[42] which can be both a push and pull factor. For example, charges tend to be a relatively more important driver of past and potential future switching for the wealthier, and the multi-homers.

3.63 While the survey found that push factors such as poor support and poor website experience were triggers to switch, our qualitative research shows that issues with the platform need to be significant and sustained to trigger a switch. Participants compared the perceived work involved against a perceived marginal benefit in some cases. This is further supported further by our consumer survey which found nearly a third (30%) of consumers had been with their platform over 9 years before they decided to switch. We found that switchers are more likely to have researched and shopped around before choosing to invest with the platform, and more likely to have researched charges.

Impact of switching on consumer outcomes

3.64 We explored whether consumers that do switch make good choices, at least in terms of price. We considered whether self-directed switchers, on average, pay lower prices than those that do not. We compared the distribution of charges[43] paid by those who have switched 'directly' in the last 3 years[44] to the distribution of charges for those who have not. We did not find evidence that charges paid differ between the 2 groups.

3.65 This exploratory analysis indicates that, on aggregate, consumers may not be switching to cheaper platforms overall. However, if consumers paid higher charges before switching, the findings could also be consistent with consumers switching to access lower charges. We explore consumer outcomes in terms of price and non-price features in Chapter 7.

Barriers to switching

3.66 Our consumer survey found that, of those that had switched without the help of an adviser in the last 3 years, 11% experienced some difficulty during the process. Yet the majority who did switch found the process easy.[45]

3.67 However most consumers (73%) have not carried out any 'direct' switching activity in the last 3 years. The main reason given by those who have not switched is that they are happy with their current platform (46%). The second most common reason given involves having longer term investments (26%).[46] This is consistent with some of the evidence from the qualitative research that some consumers are not able to separate the platform from the investment product. But it also could be consistent with consumers trying to avoid potentially losing out on tax advantages of products when they switch. Other reasons given for not switching include that it would be too much time or effort, lack of understanding of how to go about switching, and difficulties comparing platforms.[47]

---

42 In the consumer research our questions focused on the total platform charges however it is possible that consumers interpreted these questions more broadly to include other charges, or more narrowly just including platform fee/headline charge.

43 We considered the main fees charged by platforms, that is the sum of platform fees, wrapper fees and dealing charges. We did not consider fund charges.

44 We adopted a broad definition of switching encompassing all possible types of actions listed under question S6bQ1 of the Consumer Survey (Annex 3).

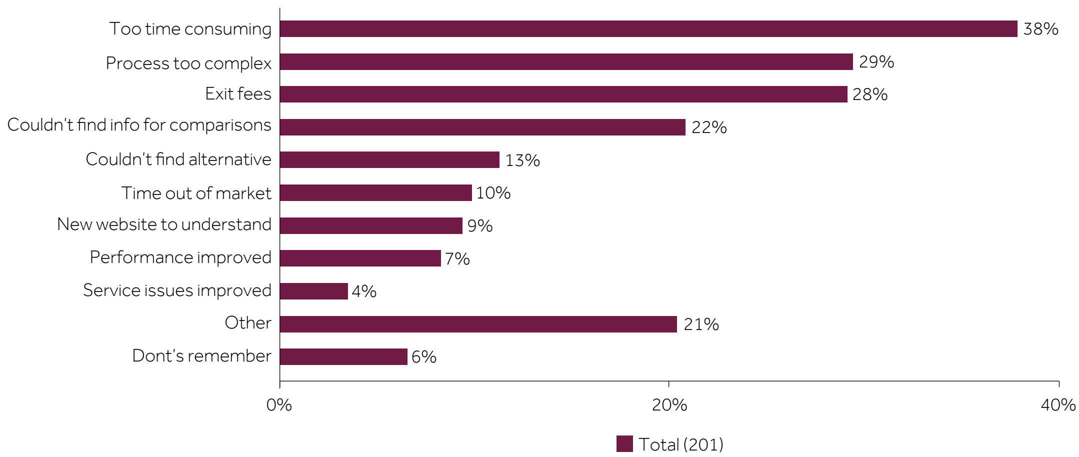
45 See Figure 44 in NMG report at Annex 2.

46 See Figure 46 in NMG report at Annex 2.

47 Those include: 'It would not be possible to move my investments', 'I wouldn't know how to switch', 'I'd never get around to it', 'I think it would cost more', 'It would take too much time and effort', 'I'd find it hard to compare platforms'' and a portion of those who selected 'other' and gave similar explanations – eg 'I'd be afraid of the risk of something going wrong'.

3.68 A further 7% of consumers tried to switch at some point but failed to do so. Figure 3.10 below shows the actual barriers that prevented these consumers from switching. The 3 main barriers were identified as the process being too time consuming, complex and the payment of exit fees. Over a third of consumers said they could not find information to compare platforms or could not find an alternative. Time out of the market was also a key barrier and in our analysis of firm responses was similarly identified as the main indirect cost to consumers. Nearly a quarter (21%) also gave 'other' reasons that included product and fund restrictions, again issues similarly identified by firms' own research.

Figure 3.10: Actual barriers to switching experienced



'Other' largely includes those who selected a new platform and attempted to switch but encountered problems such as inability to proceed without advice, product restrictions or funds not being supported

Base: Those who have been prevented from switching (see chart)
S6bQ12 What were the issues which prevented you from moving your investments away?

3.69 These barriers to switching are supported by our qualitative research. Barriers experienced by those that had tried and failed to switch also focus on time and complexity, with several saying the process should be much simpler and quicker. This contributes to a sense that it is too much hassle for the perceived benefit.

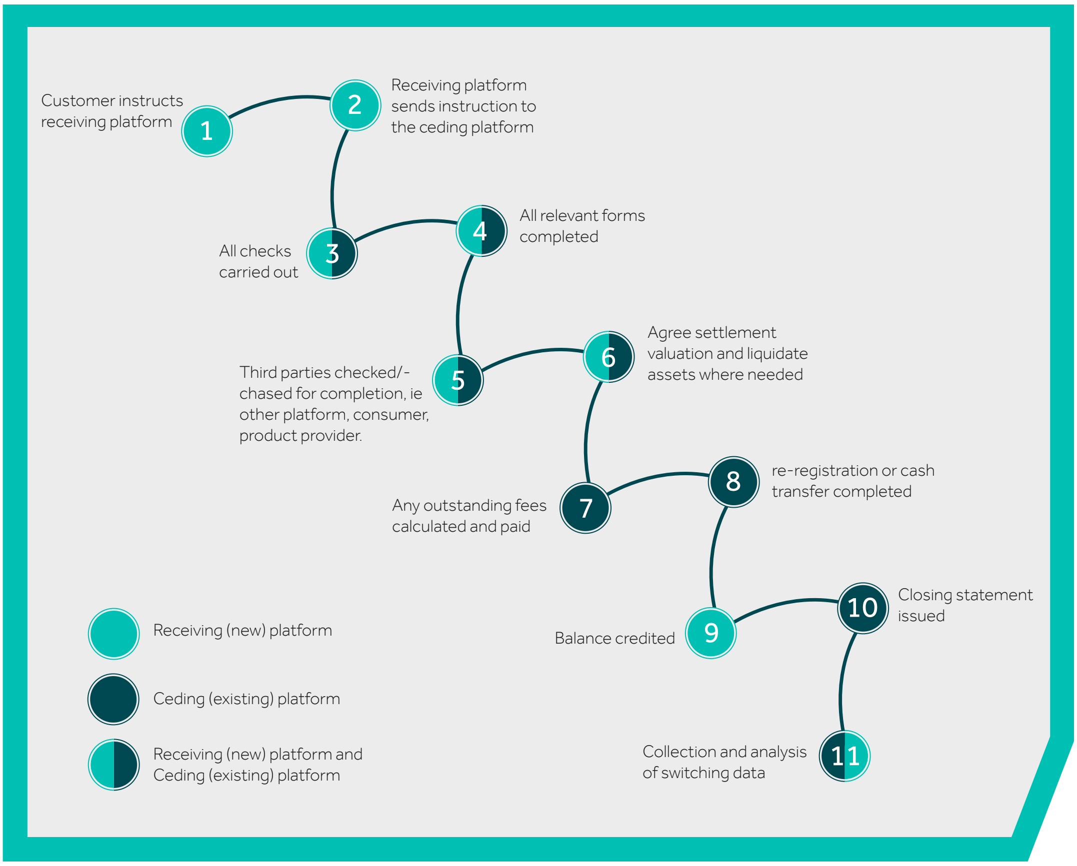
> ***"xxx service was an issue so I started looking for someone else. Xxx had better fees and were quite responsive on the email questions I sent them and I talked to them on the phone and they were very good. But I didn't do it. I decided against it because it takes forever to transfer your stocks over. Although xxx were going to pay the exit fees which I think were criminal from xxx they couldn't really tell me how long it would take. I got the impression it was how quickly xxx could provide the data points and it is not in their interest to do it so it can get held up. So I didn't do it and that is the biggest problem, I would have done it if they had said it can be done in 5 days'***
>
> ***Non-advised consumer***

Platforms' views of the switching process

3.70 As well as the impact on consumers, firms told us that switching can be burdensome and inefficient for the industry.

3.71 As Figure 3.11 below illustrates, there are a number of steps involved when switching platforms.[48] There could also be multiple stages within each of these steps and delays at any stage can have a negative cumulative effect on the switching process. While the steps to be completed are broadly the same depending on the specific product type, a number of firms said a lack of standardised process is a key issue.

Figure 3.11: An illustration of the switching process



3.72 Figure 3.12 below shows the main direct and indirect costs to consumers as well as overall barriers to switching that firms gave in their responses.

48 Indicative illustration based on information provided by firms.

Figure 3.12: Direct, indirect costs and barriers to switching

Charges

Exit fees

- Exit fees are charged by around half of the largest platforms
- Enforcing exit fees can lead to additional switching delays
- Some receiving platforms cover exit fees

Other charges

for example:
- account closure fees
- stamp duty
- additional advice fees, and
- capital gains tax

Time

Time out of the market

Consumers are vulnerable to market exposure and changes to price when assets are liquidated

Time of transfer process

Lengthy transfer process may put consumers off switching

Consumer effort

Consumers have to invest time and effort to complete switching

Driven by

Manual vs Electronic switching

- Electronic systems improve switching times but are not adopted across the market
- The process is decided by the ceding platform

Re-registration vs cash transfers

- Can be quicker to transfer cash than re-register
- But cashing out funds adds an additional valuation step

Number of third parties involved

Third party involvement means platforms do not fully control the switching process and time

Firm behaviour

Some ceding platforms may over scutinise information to delay process

Product specific issues

- ISA: notice periods to release investments
- SIPPS: additional internal process and parties involved
- Incompatible share classes or funds not being available adds barriers and can stop transfers mid-process

= Overall impact on switching levels and switching experiences.

Switching times

3.73 We found that the availability and comparability of data on switching times was generally poor. This indicates platforms do little monitoring of switching experiences.

3.74 Our analysis of the switching data available to us shows that the time to complete the process varies considerably depending on whether the process is carried out electronically or manually, whether it is an re-registration or cash transfer, and depending on the type of product.

Figure 3.13: Switching in the market

At best, switching can be completed within the same day across all product wrappers. Generally switching takes a couple of weeks to a couple of months, with some taking much longer. The longest cash and in-specie transfers are in the hundreds of working days.

Electronic re-registration transfers are significantly quicker than the manual, paper-based process. The average time to complete a SIPP paper transfer is three times as long as electronic.

Re-registrations can take significantly longer than cash transfers.

ISAs - average transfer and in-specie times broadly in line with HMRC recommendations - ie 30 working days for stocks and share ISAs. SIPPs can take significantly longer to transfer than ISAs.

Conclusions: Are barriers to switching presenting barriers to effective competition?

3.75 Overall, evidence points to significant barriers to switching. Despite the high levels of multi-homing, these barriers are likely to affect consumers' ability to switch platforms and so put enough pressure on platforms to provide continued value for money.

3.76 7% of consumers in our research say they have attempted to switch at some point but failed to do so. Consumers note significant actual and perceived barriers to switching – that the switching process is too long or complex and that they have to pay exit fees. These are the same issues that firms themselves say affect the switching process and timelines. The lack of standardisation of the switching process, the number of parties involved, the complexities around the specifics of switching various product wrappers and underlying investments are all impacting consumers' experience and ability to switch, raising barriers to switching.

4 Competition between adviser platforms

We found that platforms largely compete on the services they provide to advisers. We assessed the benefits and costs of these services and whether they have the potential to alter advisers' incentives, leading to worse outcomes for consumers.

We found that most of the services platforms offer advisers, which advisers do not pay for, directly or indirectly benefit consumers, but many advisers also use some services which may alter their incentives.

Platforms do not compete on how transparent and comparable they make fund charges. We believe doing so would directly benefit advised consumers.

There is evidence that adviser platforms compete on price to some extent, but it appears to be a less important factor than service levels.

High switching costs may mean that existing investments are left on more expensive platforms. While advisers update the list of platforms they consider for new investments over time, the level of switching for existing investments is very low. The main reason is the length of time it takes to switch, due to the complexity of the process and the lack of standardisation. As a result, provided the platform continues to meet relatively low requirements to be suitable for the client, even if there are superior alternatives that advisers tend to use for new clients, advisers very rarely switch existing investments across platforms.

Many advisers in our sample charge an extra fee for switching on top of their ongoing advice fee, negating the potential benefit of lower platform fees. The discounts some advisers achieve from platform fees typically apply to all their clients on that platform, so some existing investments also have the potential to benefit from competition for new investments.

Orphan clients who no longer have an adviser can be charged extra fees whilst having limited control over their investments. We estimate that there are currently just over 400,000 orphan clients with just over £10bn of assets on platforms, and that this figure has been rising. A minority of platforms impose extra platform fees on orphan clients, of up to 0.5% ongoing charge in addition to their pre-existing platform charges. At a minimum, we estimate that around 10,000 orphan clients are currently paying extra fees amounting to over £1.2m every year.

Introduction

4.1 This chapter summarises our analysis of how competition between adviser platforms works and the implications for consumers. We examined advised consumers' involvement with platform selection and use, how advisers select which platform(s) to use, how they use them when selected, and the extent to which advisers switch investments between platforms.

4.2 Platforms are paid for by consumers' platform fees but advisers choose the platform. Platforms offer tools and services to enable the adviser to implement investment decisions on behalf of their clients, such as buying and selling securities. They also offer tools to help advisers run their business, such as fee collection and services that allow them to operate a centralised investment proposition (CIP), and tools to help them provide financial planning, such as attitude to risk calculators and cash flow modelling.

4.3 In principle, advisers could choose platforms that best meet their own requirements rather than those that are best value for their clients. This may incentivise platforms to develop new features for the benefit of advisers rather than consumers, who may then pay for these features through higher platform fees.

4.4 We investigated how advisers balance their own requirements against the requirements of their clients when selecting and using platforms. We also looked at whether platforms offer good value to end consumers when providing services for consumers and advisers.

How involved are advised consumers?

4.5 Our consumer survey identified different types of advised consumers. The majority of these consumers delegate investment decisions to their financial adviser, while a minority of advised consumers play a partly active role in their investment decisions.

4.6 In most cases, advised consumers are presented with a platform recommendation which they tend to accept. Trust in advisers is high and less knowledgeable consumers or those that do not want to be involved in any decision making are paying for an adviser to select platforms and investments for them.

> ***"She explained it to me but whether I chose it because of that or not, I don't know. I am paying her so she is advising me and her advice has worked out alright so far."***
>
> ***Advised consumer***

4.7 As most advised consumers play a limited role in selecting their platform, our assessment in this chapter is focused on how advisers select the platforms they use for their clients' investments and what adviser platforms do to attract and retain advisers.

Evidence

4.8 In our assessment we used qualitative and quantitative evidence from responses to our Requests for Information (RFI) for platforms and advisers, as well as findings from our consumer research. We sent the adviser RFI to 235 entities and received 166 responses from non-network adviser firms, networks and Appointed Representatives (ARs) of networks.[49] In this chapter we refer to 'non-network adviser firms' as 'adviser firms'. Where we use the term 'advisers' this covers all types, including adviser firms, networks and ARs. We use 'FA' for individual financial advisers.

4.9 We do not report results separately for all types, but highlight where we found differences between them. Our aim was to get a good indication of the views of advisers of different types and sizes. However, the composition of our final sample does not reflect the composition of the adviser market, and should not be viewed as representative of the adviser market in statistical terms. We have taken this into account when interpreting the results, relying chiefly on findings that are consistent across different types of advisers.

49 We decided to exclude 1 response from the analysis as we received 2 responses from the same AR.

How do advisers select platforms?

4.10 In this section we consider whether advisers choose platforms on the basis of the platform's price, including discounts on platform fees, financial arrangements between platforms and advice firms and non-price platform features.

The role of price when advisers select platforms

4.11 When we asked advisers how they assess whether platforms provide value for money, many said platform charges are the key consideration. While advisers noted lower platform costs among improvements they had seen in the platform market since January 2014, they also think that there could be more intense competition on price.

4.12 To test whether advisers place their clients' money on platforms they think are lower cost, we asked advisers to score their platforms based on how expensive they were. We then compared this ranking to the platforms they directed flows to over a 3.5 year period.

4.13 We found that there are many more advisers placing new investments on platforms they think are relatively cheap than advisers placing new investments on platforms they think are relatively expensive. However, most also place new investments on platforms they score as mediocre on price. This implies that advisers put some of their new investments on platforms they do not believe are particularly competitive on price, indicating that price could be a less important consideration than other non-price factors. If this money is not switched in the future, it would remain on a platform that advisers do not rank highly on price.

4.14 When we asked platforms why they attract advisers, more platforms mentioned service level, range of investment options and the tools and features than cost.[50] This is consistent with advisers placing at least some of their new investments on platforms for reasons other than a low price.

4.15 Our consumer research found that platform fees do not appear to be a particularly important consideration for advised consumers compared to other, non-price features (see Figure 3.5). This suggests that advised consumers do not apply pressure on their advisers to choose the cheapest platform. Combining this with our assessment of where advisers actually place money against their views of the competitiveness of the platform's charges, we consider that while platform prices are 1 important consideration, other factors are likely to have more influence on advisers' platform choices.

4.16 New cost disclosure requirements under MiFID II (which came into force on 3 January 2018) are designed to increase scrutiny of the components of the total cost of investing, including the adviser's service, and help consumers make informed investment decisions. As consumers begin to receive costs and charges information in accordance with the new MiFID II requirements this information may drive an increased focus on adviser platform cost.

Platform fee discounts

4.17 Advisers can improve prices for their clients by negotiating platform fee discounts. Around two-thirds of advisers said they try to negotiate discounts with platforms.[51]

50 Advisers scored all platforms relatively highly on the transparency of pricing.
51 ARs tend to negotiate less because it is done at network level.

Most of those that do negotiate said that they have successfully achieved a discount on at least 1 platform. We observe that the majority of platforms offer discounts on their fees to at least some advisers' clients.[52] A minority do not offer discounts at all.

4.18 The most common condition for obtaining discounts is an adviser reaching or committing to reach a certain AUA level or to place a certain amount of AUA on the platform each year.[53] Larger advisers are more likely to successfully negotiate on platform price. The level of discounting varies widely between firms, but can be up to two-thirds off list prices. Although there are a few exceptions where discounts only apply to new money, discounts usually apply to new and existing investments and all consumers benefit from these.

4.19 Overall, therefore, some existing investments have the potential to benefit from price competition for new investments, platforms do not appear to unduly restrict discounts to future inflows and advisers of all sizes appear to be effective in getting discounts.

4.20 Although discounts in exchange for volume of business benefit the end consumer through reduced platform fees, they may also be less of an incentive for advisers to switch or consider alternative platforms that may be better for consumers. Discounts for a commitment to reach a certain volume of assets on the platform or level of inflows, and those combined with a higher service level to the adviser, are likely to act as an incentive for advisers to channel flows to existing platforms. As a result they may not consider alternative platforms which may offer better value even without discounts. Of the 47 advisers that gave a reason for not negotiating discounts, 9 said this was because they thought that discounts and the conditions to achieve and maintain them would compromise their status as independent financial advisers.

Financial arrangements between platforms and advisers

4.21 Financial arrangements to attract or retain advisers appear limited. The financial arrangements that do exist include directly or indirectly offering advisers financial help to expand their business and offering advisers a private equity stake in the business.

4.22 Such monetary arrangements need to comply with the applicable rules in COBS which govern when monetary and non-monetary benefits can be paid or received by firms. As a self-created conflict of interest, they are likely to impair advisers' ability to fulfil their duty to act honestly, fairly and professionally in the best interests of the client, even if these conflicts are adequately disclosed to clients.

The role of non-price features when advisers select platforms

4.23 Other than price, features that advisers ranked highly in importance when selecting platforms were:

- the platform's charges are clear and simple to understand
- the platform is easy and intuitive to use
- it has a wide range of wrappers and investment products to choose from
- it gives a high level of service and technical support

52 We have seen 1 example of an adviser firm introducing other fees which negate the discount it has achieved from list prices on the fees of its preferred platform, so that the benefit accrues to the firm rather than clients.

53 Other conditions platforms mentioned included efficiencies (less support or sales required from platform), quality of business (ie fewer customers with larger pot sizes) and reaching a profitability threshold for the platform.

4.24 These are features that platforms told us attract advisers to them. Based on advisers' ranking, the least important features when selecting platforms are:

- that the platform presents details of products, such as performance and price, in a way that makes it easy to compare them
- that the platform is willing to adapt to specific adviser needs, such as list funds in response to adviser demand

4.25 Functionality to make back office integration work more easily, to make client relationship management easier and to provide a good experience for clients when accessing the platform directly were ranked in the middle.

How do advisers use platforms?

4.26 In this section we explore whether advisers put pressure on platforms to improve their services and whether the services offered align with investor interests.

4.27 Platforms provide advisers with a wide range of tools and services to help them carry out and run their businesses. With very few exceptions, advisers do not pay for any of these. Platforms cover the underlying costs from revenues which they get primarily from consumers' platform fees. Advisers may therefore lack incentives to ensure that platform fees are commensurate with the service they provide to end consumers.

4.28 If platforms' tools and services make things more efficient for advisers, such as time savings in producing reports or implementing decisions, we expect these efficiencies to be passed on to the end consumer if the adviser market is working well.

Do advisers apply pressure to improve tools and services?

4.29 Advisers told us that platforms have improved their online functionality, tools and product breadth in recent years. We asked advisers to score platforms on a number of features and found that most platforms score well on the availability of wrappers and investment products, ease of use and the level of service and technical support.[54]

4.30 Around half the adviser firms in our sample said that they approach platforms with requests to improve existing tools or introduce new ones. Most said that they have seen improvements following feedback. After product expansion, the most frequently mentioned changes were Capital Gains Tax (CGT) calculators and the introduction of retirement planning tools. Both tools help advisers with financial planning. See Chapter 7 for further analysis of the improvements to platforms' tools.

4.31 Around a quarter of all advisers said that there are tools or services they would like platforms to provide but that platforms are not able or willing to do so. In most cases were tools and services that are available on many platforms, but probably not on the one the adviser uses.

4.32 There appears to be pressure from advisers to improve some tools and services to which platforms react by enhancing their offerings.

54 However, most platforms score badly on the following features: "the platform has functionality to make managing my business, back office and/or marketing easier" and "the platform has functionality to make client relationship management easier".

Are tools that are used by end consumers adequately provisioned?

4.33 We asked advised consumers what features they value when using a platform. Although a significant proportion had no view as they leave it to their adviser, they ranked access and tools to view and manage investments as the most important. This is consistent with what advisers told us about the features consumers most value, the top 3 being view holdings and valuation, hold all investments in one place and ease of administration.

4.34 Apart from viewing access, which almost all platforms make available and consider to be important, other potentially useful information for consumers like time and money weighted returns, or accessing fuller reports, is not common. Nearly all platforms have the capability to allow consumers to view their investments, but only around half allow consumers to directly access full reporting. Only around half of platforms are capable of reflecting assets held off the platform to give consumers a view of all their savings in one place.

Do tools used by advisers benefit consumers?

4.35 Most tools are used by advisers and not consumers. Here we focus on whether platform tools have clear direct or indirect benefits for consumers and on any potential to distort advisers' incentives, so to make them less likely to act in the best interest of their clients.

4.36 The table below summarises the key tools and services platforms provide to advisers. We have categorised them based on what proportion of advisers use them and include information on what proportion of platforms offer them.

Figure 4.1: Adviser platform tools and services

Tool/service	Definition	Adviser use	Platform provision
A. Charge collection	Collects adviser charges from within tax wrappers	Majority	Majority
A. Reporting and management information	Provides reports on account activity for clients and information on clients for advisers	Majority	Majority
A. Pre-funding	The platform pre-funds eg transactions before funds clear or tax relief on pension contributions	Majority	Majority
A. CGT calculator	Calculates the impact of transactions on CGT liabilities	Majority	Many
B. Continuing Professional Development (CPD)/ education	Training for advisers on platform use, legislative/ regulatory changes, business management, exam preparation	Many	Many
B. Model portfolio management	Enables a centralised investment proposition across groups of clients	Many	Many
B. Bulk rebalancing and switching	Enables a centralised investment proposition across groups of clients	Many	Many
B. White labelling	Makes the platform appear to clients under the adviser's brand	Many	Many
C. Asset allocation	Models asset allocations that accord with clients' attitude to risk	Minority	Minority
C. Fund risk profiler	Models how much risk funds take	Minority	Many
C. Risk profiling	Profiles clients' attitude to risk	Minority	Many

Tool/service	Definition	Adviser use	Platform provision
C. Retirement modelling	Models effect of returns and withdrawals on retirement plans (esp. for drawdown)	Minority	Many
C. Cash flow modelling	Models how returns and withdrawals affect future cash flows	Minority	Minority
C. Research and best-buy lists	Fund research and recommended funds	Minority	Majority for third party research, minority for in-house research and best-buy lists

Definitions: 'majority' – over 2/3, 'many' – 1/3 – 2/3, and 'minority' – less than 1/3 of respondents, excluding those who replied 'N/A'.

4.37 We consider that the first group of tools (A) that most advisers use, and most platforms provide, has little potential to distort advisers' incentives. They all appear to have tangible, if not necessarily direct benefits for their clients. It seems reasonable for advisers to choose platforms that provide good quality versions of these tools and services.

4.38 We are more concerned about the second group of tools (B), as it is unclear what benefit clients get from them and they could disincentivise advisers from switching platform. Advisers' descriptions of how these benefit their clients were mostly limited to the argument that these tools save them time or make them appear more professional.

Continuing Professional Development (CPD) and education

4.39 Financial advisers are required to get CPD and they may want more information and training on relevant topics. The provision of training is likely to be a non-monetary benefit. Training on the benefits and features of a specific financial instrument or an investment service is likely to a type of non-monetary benefit which can be provided by a platform and received by an adviser in compliance with our rules.[55]

4.40 Courses and educational material on general financial and legislative topics and exam preparation are available from 3rd party sources which may be more suitable. Training and consultancy on business management, such as telephone sales and expansion is unlikely to, for example, improve the quality of service to the end client. We note that some platforms now charge advisers for some of this material or have recently stopped providing it.

White labelling

4.41 We believe that the provision of a white labelling service can, in principle, constitute a non-monetary benefit. Although each case will depend on its own facts, we believe that a white labelling service that is offered to an adviser by a platform is likely to confer benefits upon the adviser without any clear benefits for the adviser's client. It may also promote the adviser relying on a platform. Not all platforms provide white-labelling, so advisers wanting to keep using their branding have a restricted set of platforms to choose from if they want to explore switching.

55 In the case of a platform/adviser doing non-MIFID business, see the guidance in COBS 2.3.14G and paragraph 13 in the table of guidance in COBS 2.3.15G. In the case of a platform/adviser doing MiFID business see COBS 2.3A.19R(5)(c).

4.42 Switching to another platform offering a white labelling service could disrupt the consumer's user experience in a way advisers might want to avoid. There is some evidence that providing white labelling raises costs for consumers. One firm told us it is considering restricting its white labelling service to its largest adviser firm users due to the cost providing it.

Model portfolio management and bulk rebalancing and switching capabilities

4.43 Model portfolio management and bulk rebalancing and switching capabilities make processes more efficient for the adviser and reduce errors including when they run a CIP. This could benefit the end client if these efficiencies are passed on through, for example, lower advice charges. However, as we show below, platform use doesn't generally result in lower adviser charges. Once a CIP is established on one platform, the inconvenience of re-establishing it on a new platform and switching customers may act as a barrier to switching platforms. This can mean the adviser comes to rely on the original platform selected for the operation of their business.

4.44 We think these tools can potentially distort advisers' incentives when considering which platform to choose and could create barriers to switching platform. While our assessment of advisers' choices does not suggest that the availability of these tools are key considerations for most, there still appears to be scope to align consumer and adviser interests better.

4.45 When considering which services to receive from platforms, advisers should ensure they are compliant with our non-monetary benefit rules. We set out the rules in the box below.

FCA non-monetary benefit rules

Where a product provider or a platform makes tools available to advisers, firms should be aware of the FCA's rules on paying and receiving monetary and non-monetary benefits.

Depending on the type of business being carried out by the firm the relevant rules which govern the circumstances in which a firm can pay or receive a monetary or non-monetary benefit can be found in COBS 2.3 (for firms doing non-MiFID business) and COBS 2.3A (for firms doing MiFID business). In particular, adviser firms should consider, as applicable, the provisions in COBS 2.3.1R and COBS 2.3A.15R and ensure that any payment or receipt of a monetary or non-monetary benefit satisfies any applicable conditions.

Firms should be able to satisfy themselves that the use of such tools is not expected to result in the channelling of business from the advisory firm to the provider or platform and does not need to be relied upon by the advisory firm in the future in order to continue to service its clients. When considering the provision of tools for advisers (at no cost to the adviser), platforms should also consider the guidance in, as applicable, COBS 2.3.14G, 2.3.15G and COBS 2.3A.21G and COBS 2.3A.22G.

4.46 Advisers use the last group of tools (C) less commonly. Most advisers told us that they are paying to use 3rd party versions of these tools elsewhere, which they say they prefer on the grounds of independence and consistency. These tools are aids for advisers when performing aspects of their financial planning service, and are subject to the same provisions on non-monetary benefits. We found that only a minority of adviser platforms make them available and that the cost of platforms providing these services appears relatively small compared to the overall cost base of platforms.

4.47 Overall, the tools and services that advisers and platforms focus on typically benefit the adviser with some potential indirect benefits for the consumer. However, we have concerns about the impact of some services on advisers' incentives, as all tools and services are available for advisers at no extra charge.

Tools to compare investment options and fund charges

4.48 Most advised consumers rely on their financial adviser to choose and review their investments' performance and charges. So we reviewed whether platforms are providing tools to advisers for this, as well as the pressure advisers apply to get better deals for their clients.

4.49 Advisers ranked functionalities that enable them to compare the price and performance of products among platforms' least important features. Such features also did not appear among those that platforms believe attracts advisers to them. Almost all platforms received relatively low scores on these features from advisers.

4.50 Platforms generally do not appear to show advisers the individual and weighted average fund charges their clients are paying when they view client accounts. This means that, even if advisers are assessing fund charges from 3rd parties when selecting funds, platforms are not facilitating advisers' ongoing assessment of whether the client is receiving good value for money from their portfolios.

4.51 A small minority of advisers said they negotiated fund charges with asset managers. Over half of those that gave a reason for not negotiating said that they rely on platforms to do so. This reliance on platforms is likely to be misplaced. There were only 3 adviser platforms that said that they successfully negotiate discounts with fund managers. With the exception of existing discounts being applied to new platforms acquired in mergers and acquisitions we do not see large numbers of recent discounts on adviser platforms. For more detail on the level of discounting please see Chapter 6.

4.52 Most adviser platforms have the ability to host discounts that individual adviser firms achieve from asset management groups, and to restrict access to these deals to the advisers who achieved them. At least 1 platform, however, explicitly prohibits this practice, which may prevent consumers accessing better prices.

Impact on adviser charges

4.53 We asked advisers what influence their use of platforms has had on how they determine their own fees.

4.54 The majority of advisers said they have made efficiency savings from using platforms in recent years. The saving mentioned most frequently was time. However, only a few advisers who said they made cost or time savings said they had lowered their advice charges as a result. Advisers explained that they did not lower their prices because other costs increased or because they increased their level of service. Some also said that any savings were small compared to the overall cost of giving advice.

4.55 It is clear that advisers benefit from using platforms. But without further investigation of the adviser market we cannot conclude whether these efficiency benefits are being passed on to consumers.

Switching

4.56 Here we consider when advisers switch platforms and whether there are barriers to switching. We distinguish between switching existing and new investments. For existing investments, advisers can move their client's investment from one platform to another. New investments come either from a new client or a new pot of money from an existing client. For new investments, advisers can either switch all the money to a new platform or use the new platform only for new money.

New investments

4.57 Most advisers select platforms in stages. They conduct due diligence on the platform market to select a shortlist or panel of platforms that individual FAs choose from.[56] Individual FAs then decide which platform from inside or outside the panel they should use to meet each individual client's needs.[57] FAs choose from a smaller subset of the overall panel, with some platforms reserved for existing or legacy assets only. Advisers told us they add or remove a platform because of lower platform charges, simpler platform pricing structures, cheaper fund fees, broader or specific product offerings, and lack of required functionality and poor service on the previous platform. It appears that while changes to the panel are not particularly frequent, over time advisers gradually update the panels of platforms they consider for new investments.

4.58 However, only a few advisers told us they had moved new investments to a newly added platform or away from a platform they removed from the list. The most common reason advisers cite for not changing the platforms they consider for new investments is that their existing main platform is still suitable. However, platforms' tiered pricing and the scale discounts they offer also provide advisers with incentives to place new investments on platforms they already use.

Existing investments

4.59 Although advisers consider it worthwhile to sometimes select a new platform for new investments, they rarely move existing investments from one platform to another. The majority of advisers, more than 9 in 10, say that they move an individual client's investment from one platform to another less than every 5 years.

4.60 This low level of switching was consistent with data we analysed from firms. We estimated the proportion of assets and clients that advisers switched per year using data from advisers.[58] The majority of advisers switched less than 10% of the investments held and of their clients in each period. Around half switched less than 5%, and a significant minority switched less than 1%. Data supplied by the platforms in our sample show that in 2016, 9% of new customers on adviser platforms had re-registered or transferred in from another platform, while 3% of lost customers re-registered or transferred out to a different platform.[59]

4.61 Most commonly, advisers review their choice of platform for existing clients once a year, typically for the annual review meeting with the client. The focus of the review is

56 Approximately half the firms using panels had mandatory panels, and half preferred panels.
57 Several advisers mentioned that they use third party research to assist them in the selection of platforms. Nearly all platforms indicated that they are assessed by third parties which assist advisers with due diligence. Five platforms raised some concerns around the process, as some research firms charge platforms to be researched, with those refusing not being presented as options to advisers who may consider that the research covers the whole of the market, and others are deemed to have conflicts of interest with certain platform providers. We consider there to be sufficient numbers of due diligence providers in this market for advisers to come to an informed view.
58 Based on a limited sample, as only a minority of responses contained all the necessary data.
59 These numbers are much lower when considered against the total customer base.

typically on whether the existing platform remains suitable. Many advisers indicated that the annual review very rarely leads to moving investments across platforms, unless the platform is positively unsuitable. This is a lower bar than considering whether using a different platform could improve the outcomes for the client.

4.62 The evidence we have received suggests that advisers primarily test whether the platform that is being used continues to be suitable as opposed to whether a different platform might provide a more optimal outcome for the client.

4.63 When advisers did switch existing clients' investments, there had to be a compelling reason to do so. Reasons that advisers gave for switching included:

- the client's circumstances changed significantly, eg they inherited a lot of money that meant a platform with a different pricing structure was better value
- the client needed a product or functionality that was not available on the existing platform, eg different pension drawdown options
- the adviser was unhappy with the service provided by the platform (several advisers said they bear the costs of switching themselves in these cases)[60]
- the consumer switched adviser and their existing investments were on a platform the new adviser didn't use, or the adviser decided to consolidate the consumer's investments held across multiple platforms
- the adviser joined a network that restricts the choice of platforms[61]

Barriers to switching

4.64 We asked advisers how easy they consider it is to move investments from one platform to another. About a quarter of advisers said it was difficult or very difficult.[62]

4.65 We also asked advisers to estimate the cost of switching for their clients and for themselves. Almost half of advisers who responded said that they were likely to charge clients an extra fee for switching on top of their ongoing advice fee. This extra fee may be their initial charge (ranging from 1-5% of the investment value in our sample) or an hourly rate. 36 advisers provided estimates of their costs, which ranged between £150 and £1,835, with a median of £700. 22 advisers estimated the time required as between 2 and 15 hours of combined adviser and administration time, with the median time being 6 hours.[63] These advice charges can act as a barrier to switching and cancel the financial benefits of switching platform.

4.66 Advisers who charged for switching platform beyond the ongoing service charge told us that they charged because a platform switch was a full advice event which required the production of a suitability report. Whist we recognise that advisers should be fairly paid for their work, it is not clear to us why meeting suitability requirements to switch platforms should outweigh the benefits of switching. This is particularly the case where a firm offers an ongoing suitability assessment and should therefore have up to

60 This was also observed in our qualitative research with 1 consumer specifically noting their adviser had switched due to poor service on the existing platform. The consumer was content to switch on that basis and at no cost to themselves.

61 This was supported by our qualitative research that found examples of a switch of platforms as mandated by a network. The consumer was not charged for the switch and was content with the switch based on the strength of the relationship with the adviser.

62 About half of those who responded thought it was neither particularly difficult or easy to move investments.

63 Excluding 2 outliers, 1 of 'over a week' and another of '6 hours of adviser time + 10-30 hours administration'.

date information about the client's circumstances and objectives. Advisers told us they regularly undertake due diligence on the platform market to compile their platform panels, further reducing the cost of meeting suitability requirements.[64]

4.67 The barriers to switching highlighted by advisers were consistent with those highlighted by consumers. The main cost for advisers is that the switching process is burdensome and it can take too much time. The availability of different share classes on different platforms was cited as a further complication. As discussed above, we also note that certain platform practices, such as offering volume discounts, can act as disincentives to switch platforms as can aspects of some advisers' business models which rely on platform infrastructure.

Orphan clients

4.68 Orphan clients are consumers whose investment was originally placed on a platform by an adviser but who no longer have a relationship with that adviser or any other adviser. We estimate that there are currently just over 400,000 orphan client accounts on adviser platforms (around 10% of the total) with over £10bn of assets (around 3% of the total). Between 2016 and 2017, orphan client account numbers rose by over 9%, and AUA amounts by 17%. Life companies and asset managers also have orphan clients.

4.69 Orphan clients are unlikely to benefit by staying on adviser platforms, because their ability to access and alter their investments is often restricted. Many can only sell or transfer their investments to another platform, and only through a telephone contact centre rather than online. Many platforms told us that they encourage orphan clients to find a new adviser or switch to a D2C platform, but a minority did not have an orphan client policy.

4.70 Some adviser platforms impose extra platform fees on orphan clients, of up to 0.5% in addition to their pre-existing platform charges.[65] We estimate that around 10,000 orphan clients are currently paying extra fees amounting to over £1.2m every year.

4.71 Clients can be effectively orphaned if they are paying for an ongoing advice service that their adviser is not providing. With 1 exception, platforms do not actively monitor whether there has been activity on accounts with ongoing advice charges. Where there has been no activity for some time, eg over a year, and platforms are not confirming that clients are receiving an advice service, this may mean that platforms are enabling advice fees to be collected from clients who are not getting an ongoing advice service.

64 The obligations for firms assessing suitability are set out in COBS 9.2 or COBS 9.2A depending on the type of investment involved. They require that a firm must obtain the necessary information regarding the client's knowledge and experience in the investment field relevant to the specific type of designated investment or service, financial situation, and objectives, in order to ensure that a personal recommendation or decision to trade is suitable for the client. We have set out guidance on meeting this obligation in FG 17/8: Streamlined advice and related consolidated guidance.

65 In most cases they also lose discounts negotiated by their previous adviser.

5 Complexity and transparency of fees and charges

Consumers and their advisers must be able to access and assess relevant information about platforms in order to choose between them effectively. If a lack of transparency and complexity limits consumers' ability to access and assess information they may not be able to choose the right platform. They may opt for a platform with a worse proposition (eg more expensive or does not offer the right services), and stay on this platform despite there being better options for them. They may decide not to enter the market at all, not buying investment products they would benefit from. If consumers are unable to compare platforms, competition will not work effectively.

We identified a number of concerns regarding price transparency and complexity. It is often not easy to find pricing information on a platform's website, in part because it is not in a consistent place. Most platforms charge a large number of fees and their pricing structures differ in terms of when a fee is incurred, the level of the fee and the way it is set (eg in pounds or as a percentage of the investment amount). Inconsistent language across platforms makes it harder still to identify and compare similar fees across platforms.

While it is possible that consumers' needs and behavious drive some of the differences in platforms' pricing, we have not found a convincing explanation for the level of complexity and the lack of transparency we observe. We note that some of the practices we have observed are consistent with the way firms would behave if they wanted to strategically increase complexity.

We are also concerned about the large cash balances accrued on D2C platforms. In June 2017 there was £16bn held in cash on D2C platforms, amounting to 8.8% of AUA on the platforms compared to 3.9% on adviser platforms.[66] Where consumers do want to hold cash, they may not realise the cost of this as some platforms will charge fees on their cash balance as well as any potential foregone interest or investment returns.

Introduction

5.1 Our consumer survey[67] found that nearly a third (29%) of consumers do not think that they pay platform charges, or do not know whether they pay platform charges for investing, and that many of them are unable to estimate how much they are paying. We compared responses in the consumer survey to data received from the firms of actual charges paid, and we found that 60% of consumers incorrectly over or under estimated their platform charges by at least 50%.

5.2 Advisers, in contrast, generally said that they find platforms' charges clear and simple to understand and consistently scored platforms highly on this feature. However, a notable proportion (slightly more than a quarter) thought that it is difficult or very difficult to compare charges across platforms. In addition, advisers scored platforms

66 For 2017, of the firms in our sample that provided data, £45m was held in cash ISAs compared to £162 billion in stocks and shares ISAs and £27bn held in cash outside cash ISAs.

67 As set out in Chapter 3, 3.42.

poorly on presenting details of products (such as performance and price) in a way that makes comparison easy. A notable proportion thought that it is difficult or very difficult to compare the costs and characteristics of the products (such as funds or wrappers) available on different platforms.

5.3 Given concerns stakeholders raised[68] and the harm a lack of transparency and high complexity can cause to consumers we assessed:

- the transparency of platform charges and fund charges, both before and after a consumer starts using a platform
- the complexity of platform pricing structures and charges across different platforms
- the drivers behind the level of complexity and transparency

5.4 As non-price features are also important to consumers when choosing their platform, they need to be able to match price paid to level of service they will receive. In this chapter we mainly focus on the transparency and complexity issues related to charges, but have some observations about the transparency of non-price features.

5.5 European legislation such as MiFID II and PRIIPs have introduced regulatory changes that should deal with some of the information disclosure and transparency issues that we have identified. For example, MiFID II requires firms carrying out MiFID business to provide information about "all costs and related charges"[69] and also requires costs and charges information to be aggregated so as to allow a client to understand the overall cost, the cumulative effect on the return, and thus make informed investment decisions.[70]

5.6 This type of change (and the other disclosure changes introduced by MiFID II and PRIIPs), coupled with our existing rules[71] related to providing information which is fair, clear and not misleading,[72] should help to tackle some of the transparency issues we have identified.[73]

Level of transparency

5.7 The first condition necessary for consumers to be able to make an informed decision about which platform to choose and whether it is worth switching is the availability of information on price and non-price features.

5.8 To assess the level of transparency in the market, we reviewed how a sample of platforms provide information on fees and charges at the fund and at the platform level, and also looked at what sort of information was being provided. The sample

68 Almost half of the responses to the Terms of Reference to this market study raised concerns about the complexity and lack of transparency of platform charges.

69 See COBS 2.2A.2R(1)(d).

70 See COBS 6.1ZA.11R and COBS 6.1ZA.12R.

71 As MiFID II came into effect during the course of this study our review covers the period pre and post MiFID II. However, as part of our analysis we have not looked at the accuracy of the information provided to consumers or assessed whether firms are compliant with MiFID II.

72 See COBS 4.2.1R.

73 Not all information relevant to consumers is captured by MiFID II, for example interest payable on cash balances. In accordance with our rule in CASS 7.11.32R, firms must provide their clients with a written notification if they do not pay the client all the interest earned on the client's money.

consisted of 29 platforms (16 adviser and 13 D2C platforms) across 20 firms. We relied on 3 sources of information: publicly available information on platforms' websites, examples of customer statements which platforms submitted in response to our RFI, and platforms' live demo accounts.[74]

5.9 The first of these sources helped us gauge the transparency of pricing before a consumer registers with a platform. The other 2 sources helped us understand how well consumers are able to view and engage with charging information once they have started using a platform.

5.10 Figure 5.1 below summarises the categories we used to assess each platform before and after a consumer starts using the platform, setting out what we consider to be good practice.

Figure 5.1: Components of price (at platform and fund level) transparency assessment[75]

	Category	Good practice
Before becoming a customer	Discovery	Pricing information is easy to find, eg clearly indicated and within a couple of clicks of the home page
	Coherence	All information relating to pricing appears together on a single page online (per wrapper if necessary)
	Simplicity	Pricing information is simple to understand, eg contained within concise and simple tables
	Clarity	All potential fees (eg platform, product, adviser, other) are clearly articulated and it is disclosed that underlying fund fees may apply where applicable
	Tools	It is clear, in advance of registering, what tools will be available to customers once they have registered and invested on the platform
After becoming a customer	Fees paid	The customer can see total charges (ie total platform/adviser/other and grand total) paid in the period in £
	Applicable charges	The level of fee that is applicable is clear and it is explained how this has been used to calculate charges paid for the period
	Source of payment	It is sufficiently clear where the money, to pay charges, is being taken from (eg bank account, cash balance, via direct debit)
	Breakdown	All charges paid (ie platform, adviser, other; excluding fund charges) are clearly separated and identified in online and/or paper statements
	Performance	Information on how much of the investment return has been consumed by charges paid is easy to understand (eg there is a gross and a net (of all charges) investment return figure)
	Functionality	The customer is able to customise their view online to see charges and/or performance numbers across different time periods

5.11 Our findings with respect to each of the categories are summarised below.

Before becoming a customer:

- **Discovery.** For the majority of platforms, it was obvious how to find pricing information (eg there was a 'charges and rates' page 1 click away from the homepage). However, for about a third of platforms in our sample pricing information was not straightforward to find. This was more common for adviser platforms. The

74 Where the platform was unable to provide login details to a demo account, they demonstrated how their platform works through a live account at meetings held at the platforms' offices. In a few cases dummy/practice accounts, provided by firms, had not yet matured (ie nil money/transaction/charging data) making it difficult to draw conclusions.

75 This table and the good practices it lists were developed for the purposes of analysing the market study data we received and do not constitute formal guidance.

place where detailed pricing information was contained on the website varied. We saw examples of it included under 'facts and figures', 'key facts and documents', FAQs and in the terms and conditions. Information relevant to cash balances was generally more difficult to find.

- **Coherence.** Most commonly, information on core charges was summarised on the same page with a link provided to a more detailed document that set out other fees. However, we observed a few examples where different charges, including for example information on third-party wrapper fees, fund charges and interest paid on cash was spread throughout the website, or not sufficiently identified making it difficult for consumers to find and assess total costs. Similarly, a number of platforms do not make it clear whether platform charges apply to cash balances

- **Simplicity.** We generally observed good practice of clear pricing tables with notes helping interpretation.

- **Clarity.** Platform, dealing and other fees were comprehensively included in the pricing documents. However, where third-party wrapper providers were available on the platform, their wrapper charges were typically not covered in the main pricing documents. In most cases, there was a warning included that additional third-party wrapper fees may apply but in some cases this was missing. Similarly, less than half of the platforms in our sample warned consumers in their pricing documents that underlying fund charges may apply.

- **Tools.** Most tools and services were available to view before registering. A few platforms offered a demo account for consumers to trial the platform.

After becoming a customer:
- **Fees paid.** Charges were clearly itemised (listed line by line) but seldom aggregated.

- **Applicable charges.** Overall, practice was generally poor with platforms not showing the applicable rate or how charges had been calculated. For existing customers, several platforms did not show different charges line by line (or even at all) in their statements. For example, most did not calculate the total amount of charges paid by the consumer (including any applicable third party charges). Investment performance and charges were also shown separately which makes it hard to assess how much of the performance is consumed by charges. In addition there was limited flexibility in obtaining charges for a period specified by the customer.

- **Source of payment.** The source and flow[76] of charges was often unclear from statements. While most platforms offered direct debit as a way to pay charges, others did not and set the default as payment from cash account. Some firms hold back a percentage of assets, in cash, for the purpose of fee collection while others send notice before selling down investments.

- Our analysis of firm data found that 59% of firms almost exclusively collect fees from cash balances. Our qualitative consumer research showed a small number of consumers wanting more active charging information to be provided by firms. Further, 1 firm also told us that it would be requiring platform charge fees to be paid via direct debit specifically to improve consumer awareness of charging.

76 Money in some cases flows into a secondary account before being paid to the platform.

- **Breakdown.** While many platforms listed platform and adviser charges clearly and separately line by line in their statements, poor practices are also widespread. Over a third of platforms in our sample either did not break down or even did not show charges at all in their online and/or paper statements.

- **Performance.** While some firms showed good practice, no platform enabled ready comparison between performance figures and charges, which makes it difficult to understand the impact that charges may have on investment returns. Performance and charges figures were typically kept apart.

- **Functionality.** Practice varies across firms but in general there was limited flexibility in viewing charges and performance for different time periods.

5.12 While some platforms provide information on fees and charges in a useful way, we are concerned that not all fees and charges are transparent to all investors. However, 3 platforms told us that they are proposing changes to improve transparency of costs and charges.

5.13 We will continue to consider the effectiveness of different ways of disclosing fees and charges as the market study progresses.

Level of complexity

5.14 Choosing investment products, and the best platform through which to access them, is a complex decision. Choosing the investment product itself requires assessing long-term, uncertain payoffs. When comparing platforms, the impact that fees and charges from both the product and the platform have on the value of investment can be large and are difficult to calculate, especially because the differences in cost often accumulate over potentially a long period of time, and accrue on varying pot sizes.[77]

5.15 Platforms help consumers engage with and navigate the investment product landscape. But, as providers of an additional service that consumers pay for, platforms and their charges add another layer of charging complexity which consumers need to consider when making investment choices.

5.16 Aside from the complexity of this assessment, the way fees and charges are designed and presented can add to the difficulty for consumers. To gauge the level of platform pricing complexity, we carried out a detailed review of 25 platforms' pricing structures. Overall, we found that platform pricing is complex and the differences across platforms may make comparison difficult for consumers. Below we summarise the main dimensions of the charging complexity.

5.17 With a couple of exceptions, D2C platforms tend to list between 15-35 different fees in total. Adviser platforms fall into 2 groups: about half of those we reviewed have a relatively small number of fees (1 to 7) whereas the other half has a similar number of fees to D2C platforms (15-35).[78]

77 As part of its response, 1 firm told us that it being able to clearly articulate to consumers the impact a very small difference in percentage in platform fee over a period of time was a key challenge.

78 However, many of those who have a small number of fees make third-party wrapper providers available that list a large number of different wrapper fees. Platforms should ensure that where third party charges are applicable, these are clear and transparent to consumers.

5.18 Platforms typically charge:

- a platform fee for using the platform
- a wrapper fee for having a particular investment account (eg ISA, SIPP). Where wrappers are provided by a third party, the pricing structure would not be set by the platform
- a dealing fee for buying and selling investment products such as funds and shares
- other charges depending on how the consumer uses the platform.

5.19 The platform fee is typically set either as a value in pounds ('fixed' pricing) or as a percentage of the invested amount ('ad valorem'). It often varies as the amount the consumer invests increases, eg a consumer may pay a certain fee on the first £250,000, then a lower fee on any money over that.[79] This is referred to as 'tiered pricing'. The number of tiers and the value at which the fee changes (ie bounds of the tiers) varies by platform. Some platforms do not charge a fee over a certain AUA – this is known as 'cliff' pricing.

5.20 This complexity is compounded by inconsistent language. For example, we saw examples of the platform fee called 'investor fee', 'service fee', 'quarterly payment', 'account charge', 'custody charge', 'ongoing platform and product administration charge', 'account administration fee', 'annual charge', 'monthly charge' and 'annual commission'.

5.21 Consumers also have a cash account on the platform, which they can use to pay fees and to hold cash for future investments. Some platforms apply the platform fee on any cash held on the platform, others do not. Some platforms pay interest on the cash (the level of which varies), others do not.

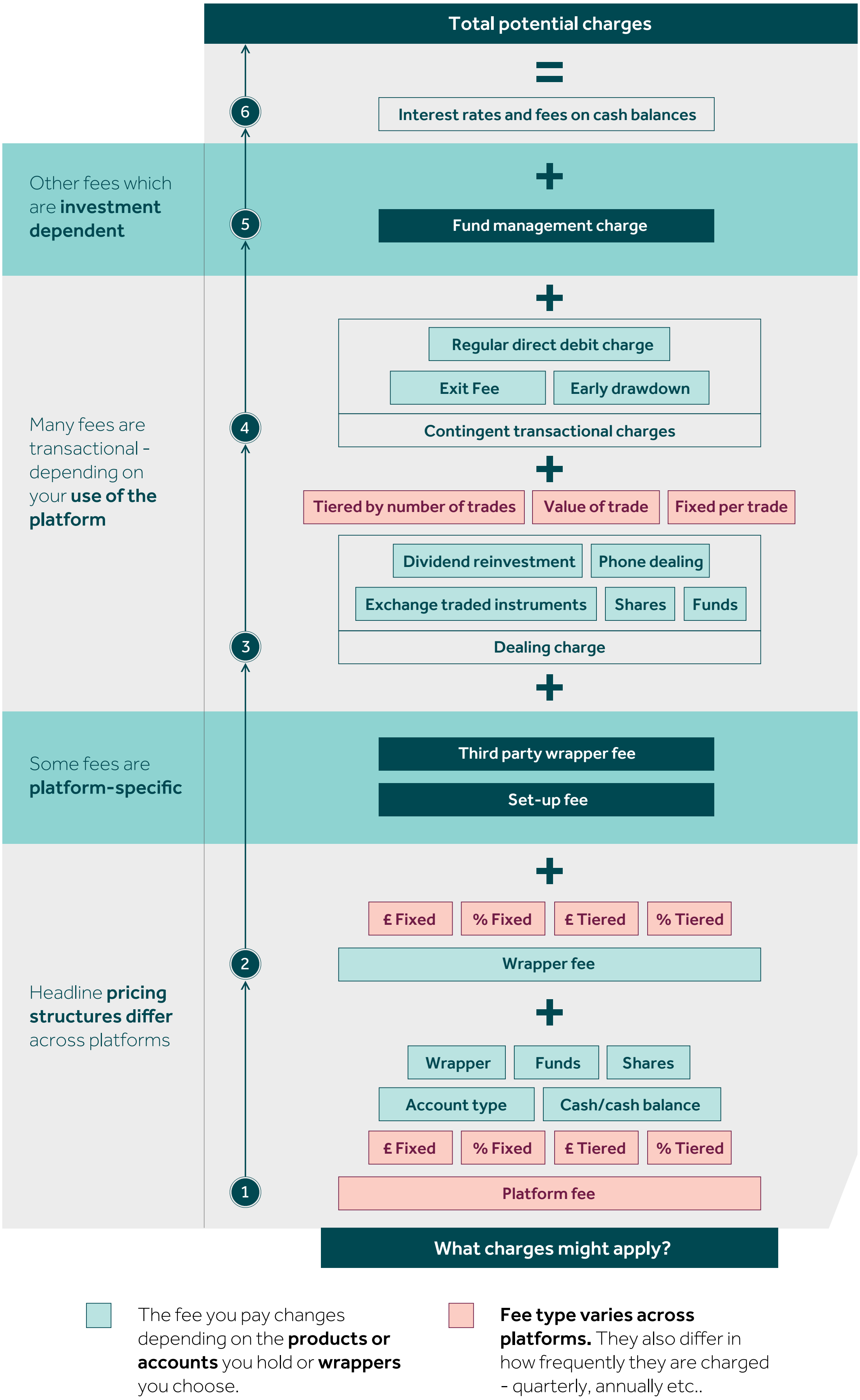
5.22 Some platforms charge a platform fee but not a wrapper fee or vice versa, whereas others charge both. The wrapper fee can also vary depending on the wrapper selected, ie fees for an ISA and a SIPP account can be different on the same platform. Most adviser platforms make a number of third-party wrapper providers available on their platform and the charging structure of these third-party wrappers will also differ from each other and the hosting platform.

5.23 Dealing charges vary depending on the product (eg funds or shares) and the wrapper on which the consumer trades. Many platforms include a small number of trades in the platform fee and charge for individual trades only afterwards. Adviser platforms typically include fund trading in the platform fee but charge fees for share trading.

5.24 Other potential charges consumers may face include fees for ordering a paper statement, dealing over the phone, valuation, exit fees, dividend reinvestment, account closure etc. These are more common on D2C than on adviser platforms.

79 Please see Chapter 7 for further analysis of pricing structures

Figure 5.2: Price complexity in investment platforms



5.25 This means that while there are usually only 1 or 2 charges (a platform fee and a wrapper fee) that the consumer will definitely pay (though the level of the charge may depend on the amount invested with the platform or in the account) there are many contingent charges that depend on how the consumer uses the platform.

5.26 There are some examples of platforms simplifying their pricing structures in recent years. For example, in May 2017, 1 platform removed all wrapper charges and transaction fees.[80]

5.27 Where consumers make a 'mistake' in their choice of platform and pay more than they would have had they been able to shop around more effectively this can be costly, since a small difference in charges accumulates over potentially a long period of time and accrues on an increasing size of investment, which can have a large impact on net returns. This is exacerbated if there are barriers to switching, because this means consumers do not easily learn from and correct their mistakes. While the ability of consumers to calculate differences in net returns over time is a broader challenge for long-term investments due to the fundamental complexity of this calculation[81], platforms should ensure that the charges themselves are clear and transparent for consumers.

Causes of complexity and lack of transparency

5.28 Financial products are often inherently complicated. They are intangible and can have many different features, and investment services and products are no exception. In this section, we consider the causes of complexity and lack of transparency beyond the inherent complexity of investment services and products.

5.29 If consumers use platforms in different ways, it is beneficial for them to have different pricing structures to choose from. We observed that some platforms are cheaper for smaller pot sizes and others are more suited for large investments. Similarly, differences in fund and share trading fees mean that some platforms are better suited for those who trade more than those who trade less and vice versa. Please see Chapter 7 for further price scenario analysis.

5.30 However, beyond different pot sizes and trading activity, it is not obvious how consumer needs could drive the differences between platforms' pricing structures. We received limited explanation from platforms on the reasons for their pricing, eg why they apply a fixed fee or a percentage. In all cases the consumer invests through an account (GIA, ISA, SIPP or other) so it is unclear how they can benefit from separate platform and wrapper fees and the variety of ways in which platforms charge for the use of the platform and wrappers.

5.31 A few adviser platforms that set a large number of fees said they do so to avoid cross-subsidisation across consumers and to make sure that the consumers pay only for the services they actually use. However, most platforms with a large number of fees did not provide any explanation and many of them said their aim was to apply a 'simple' and 'transparent' pricing structure. We do not consider these pricing structures to be simple or easily comparable across platforms.

80 Platforum, UK Adviser Platforum Pricing Guide, October 2017, page 17.

81 As part of its response, 1 firm told us that it being able to clearly articulate to consumers the impact a very small difference in percentage in platform fee over a period of time was a key challenge.

5.32 The economic literature provides theoretical and empirical evidence that it can be in firms' interest to decrease transparency and increase the level of complexity in the market. At a high level, this is because the lack of transparency and high complexity hinders consumers' ability to shop around, which then reduces the competitive pressure on firms, and they earn higher profits. Strategies that firms can apply include:

1. making it difficult for consumers to find relevant information (ie reducing transparency in general)[82]
2. making some elements of the price more complicated so that consumers do not take them into account when they choose the product (ie reducing transparency for specific price elements)[83]
3. introducing unnecessarily complex pricing structures[84]
4. making it difficult to compare prices by choosing different price frames, ie presenting prices in a way that is different from each other[85]

5.33 Some of the practices we observe are consistent with these theories. Regarding point 1 above, we are concerned about consumers being able to find relevant information, both before and after they start using a platform. There are some good practices, but we could not identify a single platform that would excel in all aspects of transparency. This is consistent with the theory that it may be in firms' interest to make it difficult for consumers to find the relevant information.

5.34 Regarding point 2 above, we do see some firms making some relevant pricing features more visible than others, which may lead consumers to make decisions based only on one part of the total cost of investing. For example, as set out above, information on interest paid on cash is often not in the same place as other fees and charges information. Cash balances are discussed in more detail in the box below. Regarding the theory in point 3 above, we reiterate our findings that platforms' pricing structures are highly complex and that in most cases we did not see a reason for this level of complexity.

5.35 As to point 4 above, we expect effective competition between firms to drive simplicity, not complexity. Firms that offer simple and easy to understand products should win consumers from those whose offer is more difficult to understand, and therefore we would usually expect competing firms to use similar conventions in their marketing materials to make comparisons easier and to highlight the benefits of their products.

5.36 To test whether this holds in the platforms market we compared the pricing structures of closest competitors.[86] None of them have similar pricing structures. They differ in the number of charges they set, varying from less than 5 to over 30, the type of

82 See, for example, Ellison, G. and Wolitzky, A., 2012. A search cost model of obfuscation. The RAND Journal of Economics, 43(3), pp.417-441.
83 See, for example, Gabaix, X. and Laibson, D., 2006. Shrouded attributes, consumer myopia, and information suppression in competitive markets. The Quarterly Journal of Economics, 121(2), pp.505-540.
84 Carlin, B.I., 2009. Strategic price complexity in retail financial markets. Journal of Financial Economics, 91(3), pp.278-287.
85 See, for example, Piccione, M. and Spiegler, R., 2012. Price competition under limited comparability. The quarterly journal of economics, 127(1), pp.97-135 or Chioveanu, I. and Zhou, J., 2013. Price competition with consumer confusion. Management Science, 59(11), pp.2450-2469.
86 We define closest competitors as platforms that both listed each other among their 5 main competitors in response to our information request.

platform fee (fixed, tiered or cliff), how it is expressed (in GBP or in percentages) and the number of tiers within the platform fee.

5.37 While consumers' needs and different usage patterns may drive some of the differences in platforms' pricing, we have not found a convincing explanation for the level of complexity and the lack of transparency we observe. Some of the practices we observe are consistent with the way firms would behave if they wanted to strategically increase complexity.

Cash balances on platforms

We have found that large cash balances accrue on platforms, and significantly more so on D2C than adviser platforms. In June 2017, there was £16bn held in cash on D2C platforms. This amounts to 8.8% of D2C AUA being held in cash, compared to 3.9% on adviser platforms. This cash could either be in a cash account, or uninvested in a wrapper; our data are not granular enough to tell us about the size of each holding type. Platform fees may be paid from cash balances.

The difference in the average size of cash balances on D2C and advised platforms suggests that advisers play a role in reducing the amount of cash the consumer holds on the platform. Large cash balances could be a reason for concern because:

- They might be indicative of the cost of holding cash (for example if a platform fee is charged) not being transparent to the consumer. Also, if the interest that platforms pay on cash is not easy to find and compare, the consumer is unlikely to be able to take this into account when choosing a platform, which reduces the pressure on platforms to offer competitive interest rates (on average, 15-19% of D2C platforms' retail revenue comes from interest earned on cash and in excess of 30% for a number of firms).
- Where the cash balances build up because the consumer has delayed making investment choices, there can be a cost in the form of foregone investment returns. While this could be a deliberate choice, we want to explore whether more should be done to remind consumers to consider the potential costs of keeping cash balances.

Third party comparison websites

5.38 Even in complex markets consumers and advisers may be able to overcome the difficulties in finding and assessing the information they need to make a good choice. One way they can be helped to do this is if the market itself provides solutions, such as comparison websites.

5.39 In exploring this possibility we completed a review of websites that compare platforms, and found that there are a few that allow consumers to enter information on how they are planning to use the platform (eg how much they will invest, in which wrapper, etc) and then rank platforms depending on what appears to be the best or cheapest for the consumer. We also found that there are a number of websites that provide summaries of platforms' offerings and/or rank them based on some criteria.

5.40 These appear to be good sources of information on the level of service they offer but not to the same extent when providing a personalised estimate of the total costs the consumer may incur. Evidence from the consumer survey shows that only a minority of consumers use price comparison websites when choosing an investment platform (only 10% of non-advised consumers indicated that they did).

6 Do platforms help consumers make good choices?

There are 2 main ways in which platforms can respond to consumer demand to help them make good investment decisions. First they can compete to offer information and tools which allow consumers to make informed decisions in relation to investment products and securities that they make available. Second they can bring down the consumer's total cost of investing by negotiating with asset managers to secure discounts and by setting up efficient trading processes.

We find that platforms could do more to enable consumers who are choosing between a wide range of investment products to take the charges of these products into account.

Platforms appear to be doing a good job for non-advised consumers who use platforms' recommended funds to help steer them towards an investment. We found platforms who are vertically integrated and have a strong incentive to promote their in-house funds do not do so in a way which would mislead investors. Best Buy lists appear to help investors pick well-performing funds. While a small number of in-house funds on Best Buy lists do not perform better than alternatives, there is evidence that investors are less likely to invest in these funds.

17% of non-advised consumers rely on their platform to narrow down and determine their investment choices by using platforms' ready-made 'model portfolios'. We have found that the information platforms make available about their model portfolios makes comparison difficult across portfolios and across platforms. Similarly-labelled model portfolios may expose investors to different underlying assets and, in turn, a wide range of return volatility which consumers may not have expected based on the level of implied risk by their model portfolio's label. We have also seen a wide range of charges and that model porfolios with higher charges have on average lower risk-adjusted net returns.

Some platforms negotiate lower prices on the funds available on the platform. We have found the prevalence of fund discounts has increased since 2013 on D2C platforms. Almost all discounts range from 1 to 50 bps. The factors that explain the size of the discounts suggest that larger platforms are able to secure larger discounts.

We have also found arrangements between a small number of platforms and asset managers which could affect the pricing of funds on other platforms. We are seeking feedback on the impact of these arrangements.

We have also found that investment platforms that provide stockbroking services to retail investors could do more to consistently achieve and demonstrate the best execution results for their customers.

Introduction

6.1 As we outlined in Chapter 3, we observed 3 general approaches to the way in which non-advised consumers choose investments on their D2C platform:

- 'Do it myself' consumers who are comfortable choosing between a wide range of investments on the platform
- 'Do it with me' consumers who are looking for a steer to help guide their investment decisions
- 'Do it for me' investors who are more willing to allow the platform to shape their investment choices on their behalf

6.2 The platforms sector caters for consumers' demand for platforms to inform their decision making. Some firms operate a more basic business model offering wrappers and funds, but with limited or no tools to guide consumers' investment decisions. Consumers on these platforms conduct their own research and make their investment decisions without assistance from the platform.

6.3 Other firms offer a wider range of functionality. These platforms help guide investors with tools or investment journeys to help them understand more about investing, what investments might work for them and which investment funds offer value for money. We discuss platform functionality and how it has changed to respond to consumer demand in more detail in Chapter 7.

6.4 If competition is working effectively we expect platforms to support different types of non-advised consumers to choose between the available investment products. In this chapter we explore this by asking the following questions:

- Do platforms help 'do it myself' investors choose between investments?
- Do platforms help 'do it with me' investors choose between investments?
- Do platforms help 'do it for me' investors choose between investments?
- What impact do platforms have on the price consumers pay for the funds available on the platform?

Do platforms help 'do it myself' investors choose investments?

6.5 Consumers who use platforms to choose between a wide range of investments need to access useful and impartial information on the main differences between investment options. Platforms are responsible for the way they present fund information to investors, although the content is usually provided by the fund manager or third party sources.

Third party information sources

6.6 Platforms provide access to third party data feeds, which give access to fund information made available by asset managers and in some cases provide information on qualitative and quantitative assessments of the funds available on the platform.

We asked platforms which third party agencies they used and whether they had any concerns about data quality and conflict of interest from the way the firm is paid – such as a 'pay to play' business model.

6.7 In general, platforms were positive about the role of third party information providers, choosing from a range of data providers with different business models. Respondents did not raise any specific concerns about the way data providers are paid or the scope of their assessments, although we are interested in any further feedback from stakeholders.

Presentation of fund information on platforms

6.8 Platforms also provide information from asset managers to help consumers choose between products. How useful this is to consumers and advisers depends on what information platforms receive from asset managers and how the platform then presents this information to the consumer or adviser.

6.9 In the Asset Management Market Study (AMMS) we found that consumers were not price sensitive to fund charges. This could be explained by fund charging information not being presented to consumers through the investment journey. In part, this could be because some platforms do not warn investors that fund charges apply. As we outlined in Chapter 5, less than half the platforms in our sample warned consumers in their pricing documents that underlying fund charges may apply.

6.10 It may also be because when fund charges are presented they are not done so in ways which encourage consumers to take them into account. Following AMMS we conducted behavioural research to understand how the way information is disclosed by intermediaries can help consumers make better choices.[87] We looked specifically at what further work could be done to encourage consumers to take fund charges into account.

6.11 A warning message appeared to increase the proportion of investors choosing a cheaper fund, particularly when it was coupled with a chart showing the impact of charges or a screen providing a summary of charges just before an investor purchased a fund. The treatments with most impact were also prominently positioned on pages that all investors had to look at.

6.12 The findings suggest that platforms can affect what consumers focus on during the investment journey.[88] They suggest there are ways in which platforms can present information about funds to encourage investors to take fund charges into account and, in turn, help to drive greater competition between asset managers.

Do platforms help 'do it with me' consumers choose investments?

6.13 As set out in Chapter 3, there is consumer demand for platforms which help consumers navigate different investment options.

6.14 There are 3 common methods used by platforms to help guide investment choices: promoting funds, constructing 'Best Buy' lists and designing a 'model portfolio' of

87 https://www.fca.org.uk/publication/occasional-papers/occasional-paper-32.pdf
88 We consider our findings to be relevant to all consumers, not just 'do it yourself' investors.

funds which meet an investor's risk tolerance. Given the impact these tools have on investors' decision making, we have looked at whether these 3 methods help consumers make good investment choices.

Promoted funds

6.15 Platforms are no longer remunerated by commission from asset managers. The main financial incentive to promote investment products is the expectation that promotions will drive flows onto the platform which will, in turn, increase platform fee revenue.

6.16 However, some firms have an incentive to promote their 'in-house' funds over other available funds. Harm may arise if consumers choose in-house funds but are not aware they are doing so, or do not take into account a wider set of alternatives which may better meet their needs. We reviewed the way in which in-house fund were presented and found no evidence to suggest that this is the case.

6.17 Platforms (and other retail intermediaries such as wealth management firms) do still earn commission from the initial public offerings (IPOs) of investment trusts and real estate investment trusts (REITs). We are aware of a number of investment trusts and REITs that paid commission to platforms at launch between January 2016 and June 2017. These commissions could be an incentive to promote the products above others on when they launch. As securities in an investment trust are retail investment products, platforms should only be remunerated for them through platform charges in compliance with our platform charging rules.[89]

'Best Buy' lists

6.18 A number of platforms in the D2C market construct 'Best Buy' lists of funds.[90] If Best Buy lists are successful in identifying funds that perform better than alternatives, they could be a useful tool to help consumers with narrowing down the selection of funds consumers can then choose between. However, there may be consumer harm if platforms are using Best Buy lists as a way to promote their in-house funds rather than to filter better value funds.

6.19 In 2017 we published an Occasional Paper which explored how Best Buy lists recommendations add value for investors, the prevalence given to in-house funds on Best Buy lists and whether in-house funds perform as well as alternative funds on the platform.

6.20 Best Buy lists do add value by identifying funds that perform better than funds not on the list. In our Occasional Paper we found that recommended funds outperform non-recommended funds by a statistically significant 0.60% per year. Investors using platform Best Buy lists to select from a narrower range of investment options which are not affiliated with the platform do appear to be currently well served by their platform.

6.21 We also examined the in-house funds included in Best Buy lists. When platforms include their own funds on Best Buy lists (and most do not), controlling for past performance, Morningstar analyst rankings, costs, and other variables, affiliated funds are significantly more likely to be added to the recommendation list than non-affiliated

89 They also earn commission from the IPOs of corporates, but as these are not retail investment products they are outside the scope of the platform charging rules in COBS 6.1E and so platforms can receive commission on these products subject to the inducements rules in COBS 2.3/2.3A.

90 Best buy lists short list funds which the platform considers to be better than other funds in that investment category.

funds. However, there is evidence to suggest that consumers are less persuaded to invest in the in-house funds that appear on Best Buy lists.

6.22 The composition of Best Buy lists has also changed in recent years. Whereas historically, actively managed funds were placed on Best Buy lists, there has been an increase in passive funds being placed on lists, although passive funds are still less represented on Best Buy lists than active.

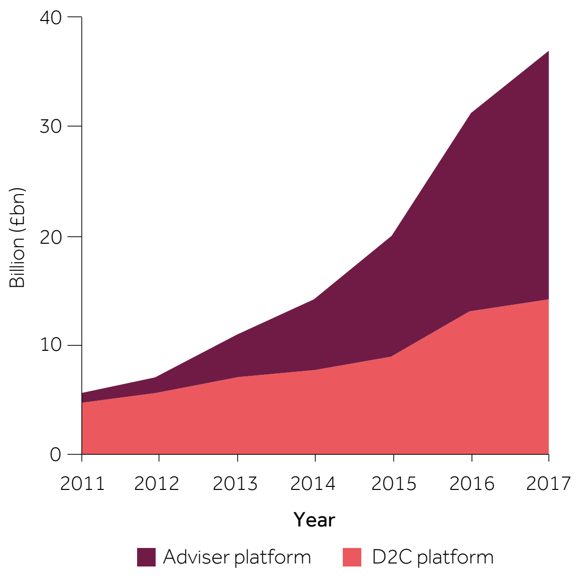
Do platforms help 'do it for me' investors make informed investment decisions?

Model portfolios

6.23 Model portfolios are designed to help make investing simpler. Investors and advisers choose a portfolio which may have a general risk label (such as 'cautious', 'balanced', 'adventurous'), with the expectation that the portfolio will expose them to a degree of risk associated with the description of that portfolio.

6.24 Platforms are increasingly designing and managing their own model portfolios. There has been steady growth in the risk-targeted model portfolios offered by platforms, with in-house model portfolio investments increasing from £5bn in 2011 to £37bn in 2017, and AUA in D2C platforms' in-house model portfolios increasing threefold (from £4.5bn to £14.1bn) in the same period. Provision on adviser platforms has increased at a quicker rate, by 25 times over the same period. From our consumer research, 17% of non-advised consumers told us that they chose model portfolios. We found similar reported levels when we restricted the sample to only those platforms which offer in-house model portfolios.[91] Such consumers are typically less active users of platforms, younger and less affluent.

Figure 6.1: AUA (£bn) in in-house risk-targeted model portfolios on platforms December 2011 to June 2017



Source: FCA analysis

91 However, as set out in Chapter 3 our analysis also found that some consumers had cited the use of these features despite the fact they are not available on their platform. This suggests a potential lack of understanding about what was meant by model portfolios and best buy lists.

6.25 We wanted to understand whether platforms enable consumers to shop around and choose the best model portfolio for them, and considered:

- whether the information platforms make available about their model portfolios allows consumers to make an informed choice
- whether the underlying asset allocations within a portfolio would meet investors' expectations given the way their model portfolio is described
- how much consumers pay to invest in a model portfolio and whether there is any relationship between charges and net returns

6.26 For the purposes of our assessment we analysed risk-targeted model portfolios, multi-asset and multi-manager funds manufactured by platforms[92] and comparable firms, collectively referred to as (ready-made) model portfolios.

Information on model portfolios

6.27 We examined the information available to consumers to assess what the platform's in-house model portfolio does and how it might meet their risk and return objectives. We analysed whether the risk labels associated with the model portfolios (including but not limited to labels such as 'cautious', 'balanced' and 'adventurous') can be used to infer the level of risk and help compare model portfolios across platforms.

6.28 We reviewed website content on model portfolios for 6 of the large D2C platforms which offer in-house model portfolios.[93] This review found that platforms differ in the number of in-house model portfolios, risk labels, and descriptions of portfolios, and even with a small number of platforms it was difficult to make comparisons between them.

6.29 Comparing model portfolios across platforms is difficult because:

- platforms present between 3 and 7 risk rated in-house portfolios[94]
- different labels are applied to explain the risk categories of the model portfolios, eg the lowest risk categories are labelled 'Cautious', 'Balanced', 'Low risk', and the highest risk categories are labelled 'Adventurous', 'Aggressive', 'High risk'[95]
- there are some examples of all the portfolios, from the lowest risk to the highest risk, having the same risk rating as each other in their KIID. This could arise because the KIID risk rating is backwards looking, and does not necessarily reflect the risk level model portfolios target for the future

92 Including portfolios manufactured by entities within the same group as the platform.

93 These firms represent nearly 60% of the D2C segment by AUA. Their in-house model portfolios comprise nearly 9% of the firms' AUA as of end 2016 (note only 5 of the 6 firms are included in this calculation as we did not have reliable data on AUA invested in model portfolios for the sixth firm). We also looked to extend the analysis to the smaller platforms but information about their in-house model portfolios was not available on the public site.

94 In some cases there are a mix of 'growth' and 'income' portfolios, but other cases each portfolio is available in both income and accumulation share classes.

95 We have seen examples, among small platforms and comparable firms, where labels are not used but instead the name of the model portfolio contains information about target asset allocation, eg "60% equity fund".

- headline portfolio descriptions are generally high level, and differ widely with some referencing broad asset class allocations, while others describe, in generic terms, target investor risk appetite, tolerance for risk, or investment horizon[96]

6.30 Model portfolios' risk categories are typically based on the underlying asset allocation, eg higher risk portfolios invest more in equities and less in bonds. We reviewed the information available to consumers to help their assessment and comparison of the risk levels of model portfolios. We found that limited and imprecise information on target asset allocations makes it difficult for consumers to understand and compare the model portfolios' potential risk exposure.

6.31 Actual asset class allocation information is generally available in KIIDs, factsheets and on the platform websites, though it is sometimes difficult to find. Target asset class allocation is even more difficult to find and often provides a broad range (eg '20-100% invested in equities').

6.32 Information available on platform in-house model portfolios' past performance is highly variable. Often there is no benchmark available, and, where there is, the benchmarks for similarly labelled portfolios varied across platforms:

- For model portfolios structured as UCITs, the majority had no benchmark declared in fund prospectuses.[97] Firms explained that, whereas single asset portfolios can broadly be assessed on their returns versus a given benchmark or peer group, model portfolios have more nuanced strategies which aim to balance income, growth, asset allocation and risk goals.

- Disclosed benchmarks included IA peer group, private peer indexes, single asset indexes such as the FTSE 100, the inflation rate and LIBOR. Others are a composite of indices but in some cases the construction of the benchmark was not clearly disclosed.

6.33 Concerns over benchmarks are not platform-specific, nor limited to model portfolios. Industry-wide concerns over the use of benchmarks were highlighted in the Asset Management Market Study (AMMS). In response to these findings, we proposed a new rule in CP18/9, which would require managers of open-ended funds to explain why they have used a specific benchmark, or alternatively explain how investors should assess fund performance. We have also proposed publishing guidance on when we expect funds to disclose benchmarks that are used for internal purposes.

6.34 The above proposals would also be relevant to platforms who structure model portfolios as unitised, open-ended funds. Platforms carrying out portfolio management services to offer non-unitised solutions are also covered under MiFID. In such cases, COBS 6.1ZA.8 EU reflects the directly applicable requirements which such platforms must comply with. For example, to establish an appropriate method of evaluation and comparison, such as a meaningful benchmark. Given that the vast majority of non-unitised solutions are exclusively for advised customers, and we have limited data on their disclosure,[98] further research is required to assess if the current

96 Eg for medium risk/balanced portfolios: "This medium-risk portfolio aims for a reasonable return with less volatility than more aggressive options", "A multi-asset portfolio holding a mixture of shares, bonds and total return funds. It should be less volatile than more adventurous options", "Middle of the range in terms of balancing risk and return. Might be suitable if you want to target healthy long-term returns and retain a reasonable bond weighting to control risk"

97 Primary prospectus information taken from Morningstar Direct.

98 Although firms did declare if non-unitised model portfolios had benchmarks, it was not always clear whether this was disclosed to investors or for internal purposes.

practices carried out by platforms help to further our policy objectives to make it easier for investors to understand the risk and return objectives of a fund.

6.35 Model portfolio charges are for the most part disclosed transparently and clearly in our sample of the largest D2C platforms. However, the total cost of investing in a model portfolio including platform and other charges is rarely easily available. We also noted that model portfolio charges can differ widely depending on whether they invest in active or in passive funds, but it is not always made clear to consumers which way the platform in-house model portfolios invest.

6.36 Overall, model portfolios offered by some of the largest D2C platforms have varying levels and quality of information available on portfolio objectives, expected risk and reward, target asset allocations, past performance, and benchmarks for performance. This makes it difficult for consumers to understand what model portfolios' objectives are and whether they match consumers' risk appetite and tolerance, and to compare model portfolios across platforms.

Underlying asset allocations

6.37 We found that naming conventions for model portfolios that imply a level of risk, such as 'cautious', 'moderate' and 'adventurous' are common across platforms. Such portfolios represent 26% of AUA invested in platforms' portfolios in 2017.[99] Consumers and their advisers expect portfolios with similar names to face similar levels of risk, and for naming conventions to help them choose. We explored whether similarly labelled model portfolios have similar underlying asset allocations and therefore expose investors to similar levels of risk.

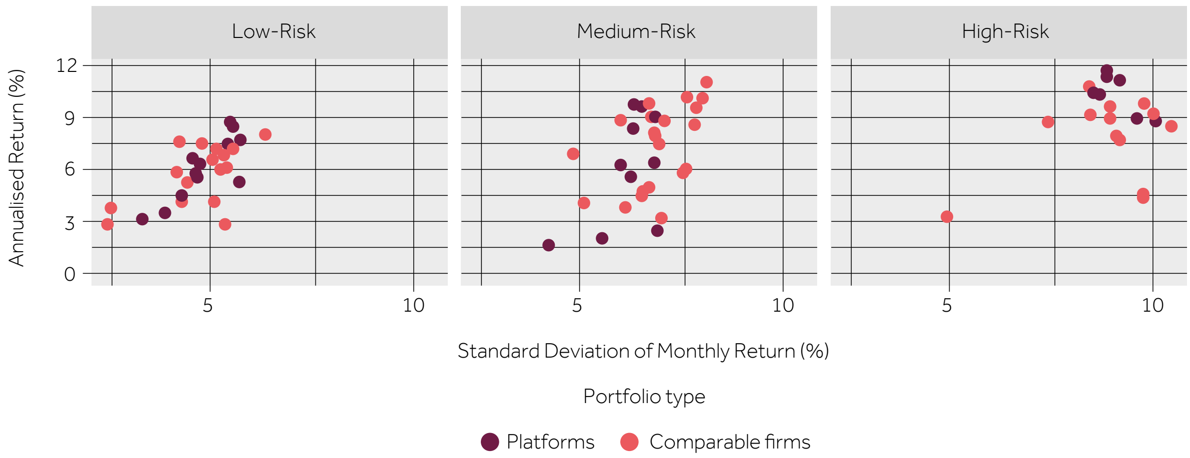
6.38 Across all naming conventions, we found inconsistency in the risk exposure when assessed by reference to asset allocation, though this was more pronounced for portfolios with medium and high risk names. For example, portfolios where the name implied medium risk, such as including words 'moderate' or 'balanced', the allocation to bonds varied substantially from less than 5% to over 60% and similar variation was found with allocation to equity (this is consistent with some of the broad target asset allocation descriptions, see paragraph 6.31). As such, many portfolios labelled as medium risk could be categorised as high risk or low risk.[100]

6.39 When assessing risk using volatility over a three-year period, we found a similar picture (see figure below). On average, portfolios experienced volatility reflective of their naming convention, with low-risk named portfolios having the lowest volatility and high-risk the highest on average. However, there was significant variation in volatility between similarly named portfolios. We also observed an overlap between naming categories, again highlighting the potential confusion caused by naming conventions.

6.40 Our findings indicate that judging risk based on naming convention does not necessarily help consumers or their advisers understand the degree of risk investors would be exposed to. At worst, such naming conventions, along with lack or inconsistency of information available on platforms, could mislead investors into portfolios with a significantly different level of risk than they expect.

99 This is 14% in AUA for portfolios from D2C platforms and 34% for adviser platforms.
100 We have also assessed the risk exposure and asset allocation of portfolios named with a "low risk" and "high risk". More details are in Annex 5.

Figure 6.2: Volatility versus Annualised Net Returns by portfolios' labels across advised and D2C platforms



Source: FCA analysis

Note: Low-risk portfolios include those labelled 'cautious', 'conservative' and 'defensive'. Medium-risk portfolios include those labelled 'moderate' and 'balanced'. High-risk portfolios include those labelled 'adventurous' and 'aggressive'. This analysis includes in-house model portfolios of D2C and adviser platforms, and of comparable firms.

6.41 The range of charges for model portfolios, both by D2C and adviser platforms, is from 0.05% to 2.5% for average charges during 2012 – 2017, with an average of 0.84%. Given the wide range of model portfolio charges, we wanted to understand if there is a relationship between charges and net returns for portfolios with similar risk levels. We have found that model portfolios with higher charges have on average lower net returns adjusted for risk, as measured by the Sharpe ratio.[101]

6.42 Taken together, the above evidence suggests that, increasingly, consumers are more dependent on their platform to narrow down and determine their investment choices and use platforms' ready-made 'model portfolios'. We found that the information platforms make available about their portfolios makes comparison difficult. Similarly labelled model portfolios expose investors to significantly different underlying assets and, in turn, a wide range of volatility which consumers may not expect. We have also found a wide range of charges.

Firm governance of tools and calculators

6.43 As part of our ongoing platform supervisory strategy, we did a multi-firm review to assess firms' governance during the design, implementation and monitoring of the tools and calculators[102] they make available to consumers who are purchasing pensions and investment accumulation products via D2C platforms. We reviewed tools and calculators of 6 D2C firms representing 68% of the market (based on AUA).

6.44 We found that the platforms included in our sample generally had appropriate governance and oversight arrangements in place during the design, launch and post implementation stages. This included identifying a clear target market, undertaking

101 The Sharpe ratio is the average return in excess of the risk-free rate per unit of volatility measured by the portfolio standard deviation.

102 The term 'tools and calculators' refers to the functionality offered by a D2C platform which enables a self-directed consumer to assess their needs, choose a wrapper or make an investment choice and/or assist them with the ongoing management of their investment.

consumer research to understand consumers' needs and making sure the tools remained appropriate.

6.45 Most of the platforms in our sample considered how to position their tools and calculators to avoid consumers' behavioural biases. We found examples of prominent warnings and platforms not making past performance the most prominent feature of research tools. However, these practices are not consistent across all platforms. We also found that platforms provide a wide range of educational materials to help consumers understand the products. Platforms generally perform root cause analysis of complaints and issues in order to improve the tools.

6.46 We identified 4 areas for improvement. Platforms should make sure they:

- include customer outcome focused measures and review them as part of the firm's senior management information
- consider vulnerable consumers[103] when designing and changing their tools
- consider the target market when making improvements/changes to tools' functionality
- consider the implications of a tool being used by consumers outside of their target market: for example, less confident or experienced investors

6.47 We assessed whether consumers were provided with fair, clear and not misleading information that the tool available on the platform is not there to give advice. We wanted to assess whether consumers could to understand the nature of the proposition enough to make an informed choice. We considered the prominence and positioning given to the description of the proposition and whether it was clearly described as guidance rather than a personal recommendation. Generally speaking, we found that consumers were provided with sufficient fair, clear and not misleading information that the tool did not give advice.

Our approach to supervision in the investment platforms sector

In our Approach to Supervision document we highlight that we're looking to be more forward-looking and pre-emptive approach in our engagement with firms, including in our approach to investment platforms. We have a pro-active intelligence-driven and data-led approach, and we take prompt and incisive action once harm has been identified.

The FCA-wide work, including supervisory work, we are taking forward in the retail investment sector is set out in our Business Plan. Our work includes assessing the impact of the Financial Advice Market Review (FAMR) and the Retail Distribution Review (RDR), reviewing high-risk and complex investments and raising awareness of fraud and scams.

103 FCA Definition: A vulnerable consumer is someone who, due to their personal circumstances, is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care.

What impact do platforms have on the price consumers pay for the funds they offer?

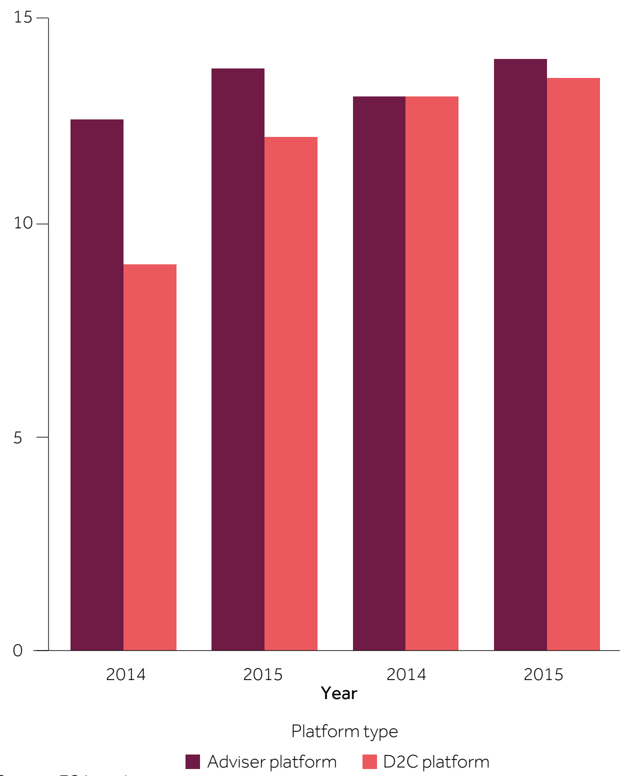
6.48 Platforms can add value to retail investors if they compete over the parts of the total cost of investing over which they have influence and control. If platforms have an incentive to use their bargaining power to negotiate down fund charges this is aligned with consumer interests and leads to better outcomes, provided there are no unnecessary restrictions on other firms' ability to get discounts and fund discounts do not become the focal point of competition at the expense of other charges.

What is the prevalence and extent of fund discounts on platforms?

6.49 We define fund discounts as the difference between the lowest OCF available across all share classes of a given fund on a specific platform and the lowest OCF most commonly occurring across platforms.[104] The focus is on discounts on one platform relative to others and not on discounts that fund managers may give to all platforms (against, for example, direct customers) as a result of the cost savings from administrative tasks platforms have undertaken.

6.50 The AUA in share classes subject to a discount has been increasing in absolute terms since 2014, from £24bn in December 2014 to £48bn in June 2017.[105] Figure 6.3 shows that around 13% of total AUA in open-ended funds across all platforms is in discounted funds. The proportion has increased only slightly over the 2014 – 2017 period, from 12% to 13% on adviser platforms and from 9% to 13% on D2C platforms.[106] These discounts are concentrated on a small number of platforms.

Figure 6.3: Percentage of AUA invested in discounted share classes of open-ended funds across platforms (%)



Source: FCA analysis

Note: The actual percentages may be slightly different from the ones presented here because our sample only covers 60 – 90% AUA in open-ended funds for smaller platforms.

104 This approach is conservative and as such may underestimate the prevalence and amount of discounts.

105 Not all discounted share classes may be available to new investors.

106 Another way to define discount is the difference between the lowest OCF available across all share classes of a given fund on a given platform and the lowest standard OCF most commonly occurring across platforms, instead of the actual OCF that may have already been discounted. Using this definition, the AUA figures only slightly increase to £25bn and £49bn respectively. When considering against the total AUA in open-ended funds, the chart below does not change with this definition of fund discounts.

6.51 70% of the discounted AUA on adviser platforms in 2017 is in share classes that were launched on these platforms before 2014. The limited number of more recently launched funds with discounts indicates limited further negotiations by adviser platforms to secure discounts from fund managers after RDR.

6.52 On the other hand, 65% of the discounted AUA on D2C platforms in 2017 is in share classes that were launched since 2014. This suggests a larger amount of more recent discounts secured by D2C platforms. However, discounted AUA is mostly concentrated on the larger platforms.

6.53 Almost all discounts across all funds available on platforms range from 1 to 50bps.[107] Among the largest 100 funds available on platforms, 33% have no discounts on any platforms, while the average discount is around 8bps with a maximum of 38bps. These discounts among the largest 100 funds account for, on average, 11% of their OCF.

What are the possible incentives for platforms to negotiate fund discounts?

6.54 Platforms may have an incentive to secure fund discounts if they give platforms an opportunity to promote those funds which, in turn, drives flows into the platform. We found that promotional activities, such as print advertising, email/website/postal marketing campaigns and highlighting of particular funds in a best-buy list, can drive significant amounts of sales into promoted funds on the platforms. The flows generated by promotions and best buy lists could be used to enhance the attractiveness of other commercial arrangements to asset managers, for example when buying books of direct business from asset managers.

6.55 They may also have an incentive to negotiate discounts if consumers over-focus on the fund charge part of the total cost of investing, allowing the platform to increase their own charges unnoticed. If this happens consumers can still end up paying more overall on a discounted fund than they would if they bought the same fund, undiscounted, elsewhere.

Do platforms have the ability to negotiate with fund managers to secure discounts?

6.56 Some platforms appear better able to negotiate with fund managers to secure discounts than others. Our aim was to understand whether or not the factors that explain this could indicate weak competition between platforms.

6.57 As noted above, discounts appear to be concentrated among a small number of the largest platforms. Our exploratory analysis of fund discount sizes indicates that larger platforms may be able to achieve larger fund discounts. We intend to carry out further empirical analysis to understand the drivers of fund discounts.

6.58 We also looked at specific arrangements some platforms have in place to secure fund discounts which could also restrict the prices of funds on other platforms. We received information about such arrangements from a number of platforms' responses to the RFI. These arrangements differed, ranging from:

- an explicit contractual clause requiring that fund prices be no higher on that platform than on comparable platforms
- a scheme to offer benefits to asset managers in return for funds not being more expensive than on other platforms, with greater benefits in return for prices better than on other platforms

107 This observation also holds for the alternative definition of fund discounts.

- expectations that discounts would be exclusive where secured as part of a negotiation without a contractual obligation
- time limited exclusive discounts in return for marketing new funds (some of which have de facto persisted after the end of the agreed period of exclusivity)

6.59 In principle arrangements like these could disincentivise fund managers from offering lower fund fees on other platforms, due to the wider impact on revenues that such an offer would have if the price also had to be reduced on a larger platform benefiting from such an arrangement. We are considering these arrangements further, and welcome views on them.

Do platforms get good prices for investors who purchase securities?

6.60 Platforms account for a large share of the retail equity market and two-fifths of total AUA on D2C platforms is in equities, almost on par with funds. If competition is working effectively, platforms should be incentivised to operate efficient trading processes and secure competitive prices on behalf of their investors who trade through the platform.

6.61 Around 95% of retail orders are executed through a network called the Retail Service Provider (RSP) system in the UK. When a consumer places an order through a platform connected to the RSP system, requests for quotes are typically sent to a number of RSP market makers either directly or more commonly via RSP hubs. The RSP market makers respond with a quote or reject the request. The RSP hubs collate the market makers' quotes and return them to the platform – either directly or through a third party broker. Depending on the configuration the client then has between 10 and 30 seconds to accept a quote and place an order.

6.62 The way platforms arrange their trading systems and carry out dealing instructions on behalf of their investors can have a significant impact on the price they achieve. Delays in trading technology, operational failures and poor system configuration result in poor outcomes for consumers. Market making firms are not obliged to supply quotes through the RSP system. Therefore, if the platform has not got contingent arrangements, consumers may not be able to trade in times of market distress.

6.63 We looked at how platforms carry out dealing instructions, how they describe them to their clients, and the steps that they take to ensure best execution. Our sample included 37 firms covering a significant portion of the retail equity trading market. Our findings cover how platforms use RSPs, monitor Best Execution and their approach to timing dealing and fund transactions.

Use of Retail Service Providers

6.64 We found that over 90% of listed security transactions were carried out through RSPs rather than through stock exchange order books, although this was rarely made clear in the platforms' descriptions of their service. Many platforms appeared to be entirely reliant on the RSP market and, in some cases, reliant on a single RSP, making it unlikely that they would be able to achieve best execution with any regularity. Around a third of platforms were unable to confirm which RSPs or even how many RSPs they obtained quotes from.

6.65 It is not clear that that platforms that connect to a single or small number of RSPs have contingency arrangements in place if, during times of market stress, the RSPs they rely on are unable to provide quotes or will only provide quotes which are significantly different from those available on other venues.

6.66 In most cases, platforms did not make clear in their order handling or best execution documentation that trades would be carried out through the RSP system. RSPs may result in better prices than other execution methods, but that is not always the case. We have previously found that firms could often improve execution outcomes if they carried out a thorough assessment of liquidity rather than solely relying on RSPs.

Monitoring best execution

6.67 In our view, most platforms do not have robust best execution monitoring arrangements. Some rely on third parties monitoring best execution, but their effectiveness is sometimes undermined by the low proportion of trades reviewed or because the price variation tolerances were so wide that only the most significant execution anomalies would be identified.

Timing of trading and fund transactions

6.68 Many platforms offer a 'pooling' option for deals in listed securities. Instead of carrying out every instruction individually for each client, requests are aggregated at security level with a single buy and a single sell deal being carried out at a fixed time in the future.

6.69 On some platforms, this is the only dealing option provided meaning that client transactions are always delayed by up to 24 hours. Where an explanation was given, platforms doing deal aggregation indicated this resulted in lower transaction costs, as the single dealing charge is spread across all the underlying clients.

6.70 There was no evidence that these platforms had considered the effect of delays on the prices clients actually achieved. The difference in price achieved by a delayed sell deal into a falling market or a delayed buy deal into a rising market would be likely to exceed any saving from the pooled broker charge.

6.71 For transactions in open ended funds, we found that many platforms make it difficult for clients to know when their trading instructions will be carried out. Policies typically state only the latest time at which a deal would be placed, often 2 business days after the request was made. It is unclear why platforms specified that length of time for placing deals.

6.72 Our assessment suggests that investment platforms that provide stockbroking services to retail investors can do more to assess available liquidity on the market to inform their venue selection and to consistently achieve and demonstrate the best execution results for their customers.

7 What consumer choices and firm strategies tell us about how competition is working

We have examined whether consumers' choice of platforms and the price and non-price features platforms offer are consistent with effective competition.

Consumers differ in their preferences and use of platforms, so if competition was working effectively we would expect platforms' price and non-price features to vary. We found that actual prices paid, as proxied by platforms' retail revenue per £ AUA, varies significantly between platforms ranging from 22bps to 54bps in 2016. We also found large differences in platform prices when we control for consumer usage patterns using a scenario analysis. Size of the pot, trading fees and wrapper fees drive the differences in the price consumers pay. Overall, there is much differentiation between platforms in terms of pricing structures and overall price levels.

We also examined whether and how platforms differentiate in terms of non-price features, such as various functionalities, tools, content, product and investment choice range, customer support, and general 'look and feel'. We observed differences across platforms in terms of non-price features. Firms also told us that they monitor and update their functionalities and tools in response to feedback and to differentiate and improve. This demonstrates that platforms seek to compete on non-price features.

We explored whether consumers appear to be making good choices and getting value for money given their preferences and how platforms differ.

For a signficant proportion of consumers, including some of the more price sensitive consumers, price is not the determining factor in their platform choice. This is not necessarily problematic and could be consistent with a market where platforms are competing effectively on the basis of price and non-price features to cater for different consumer preferences. However, taking the evidence in the round, it appears that consumer choices and outcomes are more likely to be indicative that competition is not working as well as it should. This is based in particular on evidence that the most price sensitive consumers are not choosing the cheapest platforms, on lack of price transparency and complexity, and lack of consumers' shopping around, switching, and price awareness.

The financial performance of investment platforms does not suggest widespread competition concerns in the market, as we do not find sustained excess profitability on aggregate in this market. We find there is great variability in firms' profitability, driven largely by cost differences rather than revenue differences.

Introduction

7.1 Consumers value platforms' price and non-price features. If a market is working well and firms are competing in the interests of consumers, we expect to see a range of platforms, differentiated by price and non-price features, and consumers investing via the platforms which match their preferences well.

7.2 In practice, precise measurement of consumer preferences and whether those align with the platform offering is challenging. While we may therefore not be able to make a full assessment, our analysis provides us with insight into whether the choices of platforms we observe consumers making are aligned with their preferences and hence consistent with effective competition, or whether consumers are making poor choices as a result of competition not working in the interests of consumers.

7.3 The main outcomes we look at are price and non-price features of platforms and firm profitability. In this chapter we assess:

- how platforms differentiate themselves on price and non-price features, including how non-price features change to respond to consumer needs and preferences
- whether any outcomes we observe in terms of consumer choices raise concerns that competition may not be working in the interests of consumers
- whether firm profitability and other financial indicators raise concerns that competition is not working

What do platforms compete on?

7.4 The importance platforms attach in their overall strategies to the price they charge varies. Some say that price is not the main aspect of competition, while others say they want to keep charges as low as possible. Many platforms emphasise the competitiveness of their pricing, while others consider price as part of the value for money of their offering. This indicates that platforms compete on both price and non-price features, though the emphasis differs across platforms.

How do platforms differ on price?

7.5 Platform charging is complicated and measuring it is challenging given the different profiles and consumers' usage patterns. Below is an overview of average prices actually paid, estimated using financial data. Additionally, we simulate overall price for hypothetical consumer usage scenarios so we can compare price differentiation for different charging structures by taking out any differences in consumer usage.

Actual price paid proxy

7.6 To aggregate the numerous different fees and charges paid by consumers we created a 'price proxy' for platforms based on their total retail revenue divided by average AUA[108] for each year. Despite some limitations,[109] the price proxy is a useful indicator of average overall price paid by consumers, inclusive of headline platform fees,[110] wrapper charges, transaction fees, retained interest on cash and other miscellaneous charges.[111] Our analysis is based on a sample of 25 platforms (15 adviser and 10 D2C platforms).

7.7 We found that retail revenue per £ AUA in 2016 ranged from 0.22% to 0.54% across platforms The weighted average figures for adviser and D2C platforms for 2016 were

108 A simple average of start of year AUA and end of year AUA.
109 See Annex 4 for further details.
110 For earlier years we included fund manager commission rebates as retail revenue to ensure comparability across years and firms.
111 This calculation only includes fees and charges levied by the platform for its services and therefore does not include other charges payable across the value chain such as advice or fund management fees (fund charges).

0.30% and 0.34% respectively. Price dispersion is lower for adviser platforms than for D2C platforms.

7.8 We observed that weighted average prices, as measured by retail revenue per AUA, have fallen by 4bps in the period from 2013 to 2016.[112] We note however that weighted average retail revenue in pounds per customer has remained relatively flat over the same time period, indicating that the decrease of retail revenue per AUA does not necessarily mean falling prices in the platforms market.[113]

Price scenarios

7.9 Fee structures and levels are complicated, so we simulated the levels and range of platform prices for a number of hypothetical customer usage scenarios. This enables us to compare platform pricing on a like for like basis.

7.10 We used data from firms to construct realistic usage scenarios for the price analysis. The scenarios use different pot sizes, investments in wrappers, investments in funds and shares, frequency of trading funds and shares, number of funds or shares held ('number of holdings' in the table below), cash, and tenure. The 9 scenarios are summarised in Figure 7.1 below and further details are provided in Annex 6.

Figure 7.1: Scenarios for price analysis

Scenarios	1	2	3	4	5
Descriptions	– £5,000 – ISA only – No trading and smallest number of holdings	– £13,000 – ISA only – Medium amount in shares – No trading and smaller number of holdings	– £13,000 – ISA only – Larger amount in shares – Some trading and small number of holdings	– £40,000 – Use all 3 wrappers – Medium amount in shares – No trading and small number of holdings	– £40,000 – Use all 3 wrappers – Larger amount in shares – Some trading and medium number of holdings

Scenarios	6	7	8	9
Descriptions	– £100,000 – Use all 3 wrappers – Medium amount in shares – No trading and medium number of holdings	– £100,000 – Use all 3 wrappers – Highest amount in shares – Highest amount of trading and highest number of holdings	– £250,000 – Use all 3 wrappers – Minimal amount in shares – Some trading in funds only and larger number of holdings	– £500,000 – Use all 3 wrappers – Minimal amount in shares – Some trading in funds only and larger number of holdings

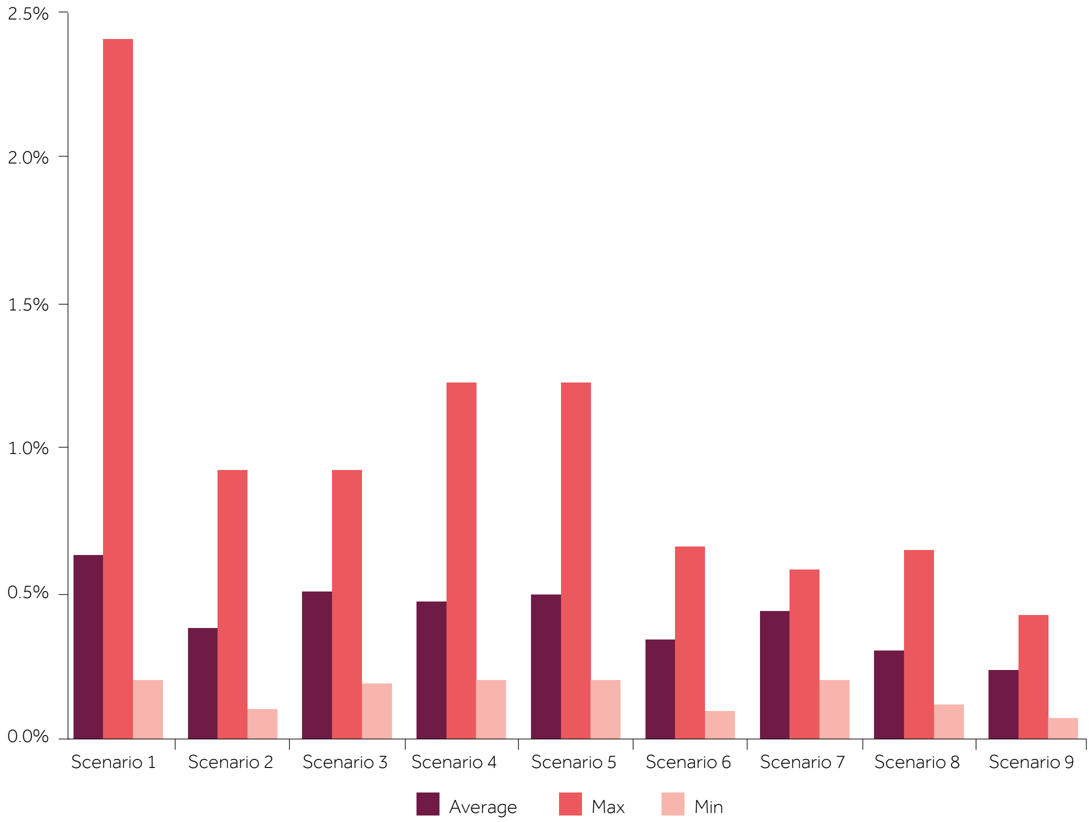
Source: FCA analysis

7.11 We calculated the total platform fees (including the headline platform fee, dealing charge and wrapper fee and subtracting any interest paid if available) for these 9 scenarios on D2C platforms only. Figure 7.2 below shows the average and the range of total platform fees, relative to amount invested ('pot size'), for each scenario on D2C platforms.

112 We also asked firms to supply their own calculated average fees paid by consumers and these figures show the same trend with average prices falling from 0.37% to 0.31%% over the same period.

113 See Annex 4 for further details.

Figure 7.2: Price scenario analysis: total platform fee relative to amount invested for D2C platforms



Source: FCA analysis

7.12 Across all D2C platforms, there is a wide range of charges for a given scenario, with the maximum fees being 3 to 12 times higher than the minimum across the scenarios. This means that a consumer with a given usage profile could be paying many times more on some platforms compared to other platforms. We observe the largest variation in platform fees for the smallest pot of £5,000, from 0.2% to 2.4% and averaging at 0.6%. Average charges across all D2C platforms for a given scenario do not vary that much and are more stable at around 0.3% to 0.5%, for most scenarios.

7.13 The main drivers of price differences between platforms are:

- flat fee structures with fixed amount in pounds for either the headline platform fee or wrapper fee, at the current levels, can make some platforms significantly more expensive than platforms with ad valorem pricing, especially for smaller investment pots
- differences in platform fee structures with some applying certain charges (eg a separate wrapper fee) while others do not
- variation in fee levels also contributes to the variation in total platform fees

7.14 Pot size and wrapper choice are key determinants of the total platform charges paid by consumers. If we compare Scenario 1 of a £5,000 pot to Scenario 2 of £13,000, the fees as a proportion of pot size reduce by 2 to 2.6 times, as some platforms have a flat fee structure.[114] Pot size greatly affects the charges consumers pay, and SIPP accounts are generally more expensive than ISA and GIA accounts, as illustrated by comparing total charges for Scenario 2 (without a SIPP account) and Scenario 4 (with a SIPP account).

7.15 Dealing charges can also represent a large proportion of total platform charges not only for consumers who trade frequently (Scenario 7) but also for those who have smaller pots and trade occasionally (Scenario 3). Dealing charges account for around a third of the price paid on average for these scenarios, compared to 12% or less on average for the other scenarios with trading activity (see Annex 6 for further details).

7.16 Our price scenario analysis highlights how platform fees vary significantly across platforms for the same customer usage pattern. It appears that pot size, product wrapper and fund and share trading frequency make the most difference to the overall platform fee. The different charging structures and the resulting overall fee levels highlight that some consumers may be better off on some platforms than on others and that it is important for consumers to be able to take charges into account.

How platforms differ on non-price features

7.17 Consumers value platforms' non-price features, the provision and quality of platform features and tools. Given this, we analysed the ways in which platforms appear to differentiate themselves based on non-price features to assess whether platforms are responding to consumer demand.

Non-price features on D2C platforms

7.18 Many D2C platforms said the quality of the service set them apart. They told us they make regular technology improvements, offer more digital access and a wider range of products.

7.19 We analysed the following groups of non-price features for D2C platforms:

- tools to manage existing investments, tools and features to help investment decisions, ready-made portfolios and lists of suggested funds
- look and feel of the online system, and availability of mobile apps
- range of information available on investment choices and products
- availability of customer support
- product range, including wrappers and investment products

7.20 We assessed individual tools and functionality in each group, looking at firm data, supplemented by our review of platforms' interfaces and public websites. We grouped platforms by their provision of non-price features – basic, standard or extensive. Our methodology is explained in Annex 6.

7.21 We found greater variation in the following non-price features of D2C platforms:

114 This is because with flat fee structure, consumers pay the same fixed amount in pound regardless of their investment size. Therefore, consumers with a larger investment pot pay a smaller proportion of their investment in platform fees, if compared to consumers with a smaller pot.

- **Ready-made portfolios and lists of suggested funds.** We saw the most variation in the availability of ready-made portfolios. These are offered by over half of D2C platforms. Lists of suggested funds are available on 9 platforms. Only 7 platforms offer both ready-made portfolios and lists of suggested funds.

- **Customer support.** Nearly all platforms offer telephone and online customer support, although the type of online support varied. Some platforms offer just secure messaging, or email or webchat, while others have a combination.

- **Range of information available on investment choices and products.** Whilst most D2C platforms provide third-party research material, often in combination with in-house offerings, we found greater variation in the style of material provided. There is differentiation across platforms in terms of the detail or quantity of research provided by platforms.[115]

7.22 We found less variation in these categories:

- **Tools to help investment decisions.** Features to help consumers make investment decisions varied slightly with some only provided by a few D2C platforms. For example, retirement modelling tools[116] are available on just 3 platforms. Fund risk profilers[117] are more common, available on over half of platforms.

- **Tools to manage existing investments.** Basic tools were common to all 22 D2C platforms reviewed whilst other tools were more rare. Downloadable performance reports are offered by 5 platforms and a CGT calculator by only 1.

- **Look and feel of the online system.** 15 out of the 22 D2C platforms have a website optimised for tablets and smartphones, and 12 have a dedicated app. Most platforms provide resources that are straightforward to find and deliver accessible information. However, 'look and feel' is also influenced by tone of language and by visual style not captured by our assessment.

- **Product range, including wrappers and investment products.** Most platforms have 2 to 3 wrappers, with their own SIPP wrapper or access to a SIPP provided by a third party. There is more differentiation in the range of investment choices (e.g. funds, shares and other exchange-traded products) offered across D2C platforms. Many offered all 3 types but a significant minority offered funds only. Some platforms offered only a smaller, selected list of investment products.

7.23 Overall we found that platform functionalities appear relatively consistent across platforms, though there is some differentiation. The differentiation in 'look and feel' between platforms could meet different consumers' individual preferences and ways of using platforms, which are difficult to capture using any objective metrics.

Non-price features on adviser platforms

7.24 Adviser platforms told us they differentiate themselves by:

115 However, the majority of research content is publicly accessible via platform public websites so consumers of 1 platform could access the research content of a different platform but, we do not know how common such behaviour is.

116 Retirement planning tools take account of the pension flexibility rules, tax implications, risk appetite and how long their money will last.

117 Fund risk profiler is a comparison tool of fund performance against other funds and/or benchmarks.

- focusing on technical support and the quality of the service they offer to adviser firms
- focusing on the nature of the technology they offer
- offering a range of in-house services, including stockbroking and SIPPs, and pre-funding

7.25 There is little variation across adviser platforms on essential functionalities and tools they offer advisers, but some features do vary:[118]

- CGT calculators are provided by more than half of the 26 adviser platforms reviewed, and half have functionality for the inclusion of off-platform assets in online reporting.
- Many platforms provide tools to help make investment choices such as separate risk profilers and fund risk profilers, with 8 platforms offering both.
- Many adviser platforms also provide research material, with third party research more common than in-house research, provided by 19 and 3 adviser platforms respectively.
- Adviser platforms differ in the level of support available. We found that almost all adviser platforms offer telephone support to advisers and end consumers, but that just over half offer online customer support to end consumers.

7.26 We cross-checked our findings with existing platform reviews by the third-party firm lang cat.[119] The lang cat platform market scorecard[120] covers a range of categories of non-price features. lang cat scores were broadly consistent with our findings. Differences in functionality levels, as confirmed by lang cat scores, are small. The largest variation between D2C and advised platforms is the type of tools offered, eg with adviser platforms more likely to provide CGT calculators.

Do platforms' features and tools respond to consumer needs?

7.27 Most firms actively consider the use and value of tools and functionality they offer consumers:

- many have monitoring or research into the tools and calculators they offer, ranging from the collection of usage statistics to routine research commissioned from third parties
- some platforms do consumer testing to check awareness and understanding of the tools and calculators they provide

7.28 The majority of firms had made changes to their tools and functionality over the past 3 years. Some made significant changes including introducing financial health and budgeting tools, calculators for specific products which illustrate potential returns,

118 Further information about adviser platform tools and services is provided in Figure 4.1.

119 We were unable to take a similar approach for D2C platforms because there are currently no external comprehensive reviews of these platforms.

120 "lang cat platform market scorecard Q1 2017", p. 13, graded 18 adviser platforms across different categories from 0 (lowest) to 4 (highest), using data collected in Q1 2017. The categories scored include features such as prefunding, portfolio management, keeping client informed, in-retirement functionality, and planning tools. lang cat note that their functionality assessment is deliberately simplistic. A high score, indicating the full range of functionality, does not necessarily mean that the provider is the most suitable offering for the client.

and mobile app launches or added capabilities for their existing mobile apps. Most had made more minor changes such as better search functionality and streamlining navigation.

7.29 Most adviser platform changes come from adviser feedback. Many adviser platforms have introduced changes to financial planning tools and CGT calculators following the pension freedoms.

7.30 Just over half of firm respondents are considering specific changes over the next few years, and a small number of firm respondents said they would continue to monitor feedback and make more changes in the future. We did not see evidence of firms planning major innovations.

Conclusions on price and non-price differentiation

7.31 Actual prices paid by consumers vary across platforms, with more variation among D2C platforms than adviser platforms. Consumers could pay very different prices depending on the platform they use. There is more difference between D2C platforms than between adviser platforms in terms of non-price features. There could be further differentiation not captured by our analysis depending on how consumers see the 'look and feel' of different platforms.

Are consumer choices of platforms consistent with effective competition?

7.32 In this section we explore how well platform differentiation reflects different consumer preferences, and whether consumers can identify the right platform for their needs and preferences.

7.33 We look at price and non-price outcomes in 2 ways:

- We map the price and non-price features platforms offer, and assess whether there is a positive relationship between them, with more expensive platforms offering a greater range of non-price features. A positive relationship between price and non-price features is consistent with firms competing to offer consumers value for money, on aggregate.
- We use customer data to explore how well consumer preferences match their platform choices, focusing on price.

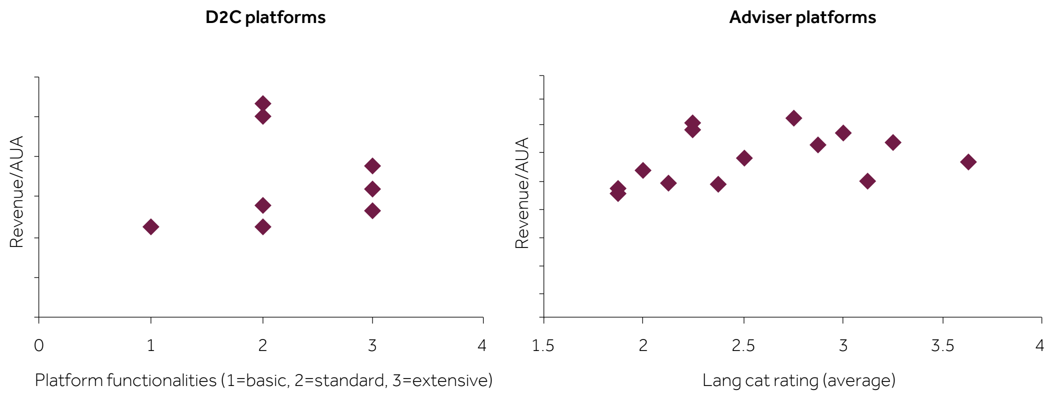
What is the distribution of price and non-price features?

7.34 Below we map the price and non-price features platforms offer. For price, we used actual price paid proxy (revenue per £ AUA, described in paragraphs 7.6 to 7.8 above). For non-price features of D2C platforms, we used platform functionality categories of 'basic', 'standard', and 'extensive' – these are based on our assessment of platform functionalities, content, product and investment choice range. For adviser platforms we use average lang cat rating as a proxy for the level of platform functionalities (see paragraph 7.26). Annex 6 contains further details of our analysis.

7.35 Figure 7.3 below shows the price paid proxy against our platform functionality ranking. For the 10 D2C platforms for which we have revenue data available, we can see that the more expensive platforms tend to have a higher level of platform functionality. Larger platforms (in terms of market share) tend to be at the more expensive and higher functionality end of the spectrum. For the 14 adviser platforms in our sample, there is a similar pattern, although some larger platforms are more expensive for a similar level of platform functionality.

7.36 We did not find poor value for money to any significant degree in aggregate. We do not find many platforms charging high prices for relatively low level of non-price features. We also observe a greater range of prices and platform functionalities for D2C platforms than for adviser platforms.

Figure 7.3: Platform functionalities vs. actual price paid proxy



Source: FCA analysis

7.37 We carried out sensitivity checks using alternative price and non-price metrics for D2C platforms (see Annex 6), and we see a similar pattern – ie higher priced platforms tend to offer more platform functionality or have a higher net promoter score.[121] For some metrics there are minor exceptions whereby relatively small platforms tend to be high priced yet offer fairly 'basic' level of non-price functionalities. This could be explained by the platform being 'niche' or having non-price features valued by customers but not captured by our metrics.

7.38 We also explored which platforms gain market share and have higher sales (ie new money invested) and whether that matched price or functionality, but we did not see any meaningful patterns.

7.39 Using price scenario simulations described in paragraphs 7.9 to 7.16, we assessed the distribution of consumers by pot size for each platform, to understand whether platforms have customers suited to their fee structure and levels.[122] We found many examples of platforms having more customers with pot sizes appropriate for their fee structure when compared to overall pot size distribution across all platforms. For example, several D2C platforms that are among the cheapest options for most scenarios with small to average pot sizes have a significantly higher proportion of customers in smaller pots of £5,000 to £40,000 compared to the overall D2C platform customer distribution.

7.40 However there are also examples of consumers on expensive platforms given their pot size. For example, 1 platform, despite being more expensive than other platforms for pot sizes of £40,000 and above, has consumers spread across multiple buckets

121 Net promoter score is a metric of customer satisfaction, measured using our consumer survey.
122 Determined by how cheap or expensive their fees are relative to other platforms across all scenarios.

between £0 – £500,000, instead of having the majority of their consumers in pot size of less than £40,000.

7.41 On average platforms tend to have more consumers with pot sizes appropriate for their fee structures.[123] But there are still many customers on platforms which are expensive for their pot size. For instance, platforms that are cheaper for larger pots still have a significant proportion of consumers with smaller pots. This may be due to the different consumer preferences for quality and services offered by platforms which are not captured by this analysis. But it also suggests that some consumers may be finding it difficult to shop around on price.

Are consumers choosing platforms consistent with their preferences?

7.42 One measure of whether a market is working well is whether consumers are choosing platforms in line with their preferences. Consumers might find it difficult to choose platforms that match their preferences in markets where products and pricing are complex or lack transparency, or where there are search or switching costs.

7.43 To test whether consumers are choosing platforms in line with their preferences we assessed:

- On aggregate, do consumers with different preferences choose different platforms?
- Do individual consumers make choices in line with their preferences, focusing on price in particular?

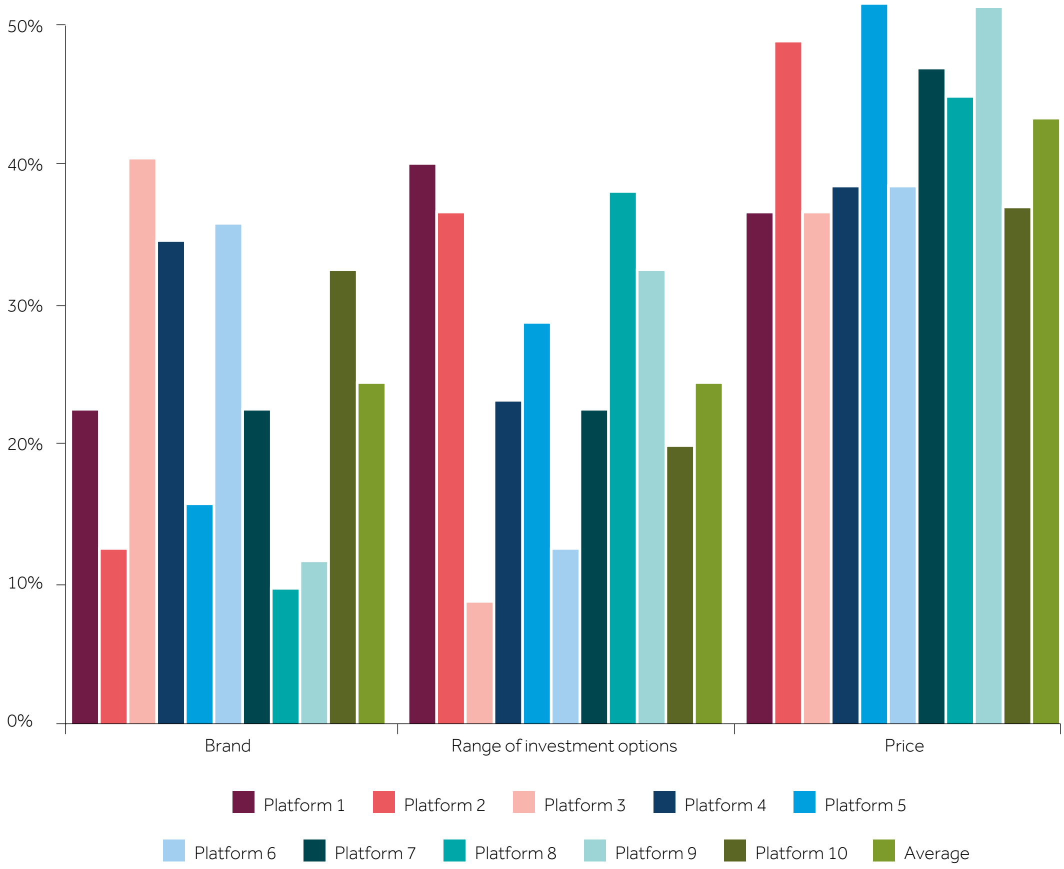
7.44 Further details of this analysis, which is based on conjoint data from our consumer survey and data from firms, is set out in Annex 8.

Do consumers with different preferences choose different platforms?

7.45 We examined the distribution of consumers with different preferences across D2C platforms. We grouped consumers into 6 different types depending upon which price or non-price attribute the conjoint analysis suggests is the most important to them.

123 Compared to pot size distribution overall in the market.

Figure 7.4: Distribution of consumers across platforms in terms of their preferences



7.46 Figure 7.4 shows the distribution of consumers across platforms, showing only the 3 most important attributes – price, brand and range of investment options. We observe the following:

- For consumers who have the strongest preference for low prices, there is little evidence that they favour a particular platform over another.
- However, we see much bigger differences in the choices made by consumers who value brand most highly. Similarly, we also see large differences in the choices made by consumers for whom the range of investment options is the most important attribute.

7.47 We then looked to see if there were any differences in the choices of D2C platforms made by consumers with the highest and the lowest preference for low prices.[124] We found that all platforms contain high proportions of both the most and the least price sensitive of consumers in our sample.

7.48 This suggests that consumers with a strong preference for low prices are making similar choices to those who prefer non-price features. Given that platforms differ in terms of price, this suggests either that there are obstacles to consumers making choices on the basis of price, or that even the most price sensitive of consumers prefer to make choices largely on the basis of non-price attributes.

124 Consumers were ranked according to how highly they valued low prices. Those customers whose ranking places them in the top 25% we define as "price sensitive", while those whose ranking puts them in the bottom 25% we define as "non-price sensitive".

7.49 For consumers who have a strong preference for non-price features there is some evidence that consumers may be choosing in line with their preferences. In particular there is some evidence that consumers with strong preferences for brand are making different choices to those with strong preferences for portfolio choice.

Do individual consumers make choices in line with their preferences?

7.50 We next explored the extent to which individual consumers are making choices in line with their preferences, focusing on price. We examined whether the most price sensitive D2C consumers are more likely to choose a lower price platform than less price sensitive consumers.[125] If price sensitive consumers are making choices in line with their strong preference for price we would expect the probability of them choosing a lower priced platform (or avoiding a higher priced platform) to be greater than for other consumers.

7.51 We used 2 alternative benchmarks for less price sensitive consumers: the sample population as whole; and the most non-price sensitive consumers (defined as those whose preferences for low price places them in the lowest 25% of consumers in our sample). For further details about our methodology see Annex 8.

7.52 We looked at whether the most and least price sensitive consumers make different decisions to the sample population as a whole. Our analysis shown in Figure 7.5 below suggests that the choice of platforms made by price sensitive[126 127] and super-price sensitive[128] consumers are similar both to non-price sensitive consumers and to the sample population as whole. For example, 68% price sensitive consumers avoid higher price platforms compared to 62% for non-price sensitive consumers. Non-price sensitive customers do however appear to be less likely to choose a lower price platform than the sample population as a whole.

125 We focus on price only since non-price features of platforms are difficult to assess. Although objective measures can be estimated for some platform features, many of the most important features are inherently subjective (eg brand), while for others customers disagree on what particular features are important (eg some consumers prefer a more limited and restricted choice of portfolios whereas other prefer to have a wider range of choice of funds).

126 Defined as consumers whose preference for low price ranks them in the top 25% of all consumers in our sample.

127 We grouped platforms into 3 categories: "lower price", "medium price" and "higher price". Which category a platform was placed in varied with the size of the consumer's investment pot (see appendix 8 for more details).

128 Defined as consumers whose preference for low price ranks then in the top 10% of all consumers in our sample.

Figure 7.5: Conjoint analysis: platform choices based on price, by consumer price-sensitivity[129]

	Avoid a higher priced platform[130]	Choose a lower priced platform
All consumers	**63%**	**17%**
Super price sensitive consumers (top 10% in terms of preference for low price)	67%	17%
Price sensitive consumers (top 25% in terms of preference for low price)	68%	19%
Intermediate consumers (middle 50% percentile in terms of preference for low price)	61%	18%
Non-price sensitive consumers (bottom 25% in terms of preference for low price)	62%	12%*
Super non-price sensitive consumers (bottom 10% in terms of preference for low price)	65%	9%*

*= statistically different from the sample population as a whole at the 5% level of significance.

7.53 We also examined whether the probability that a price sensitive consumer will avoid choosing a higher priced platform is linked to their behaviours, attitudes, or knowledge.[131] Although sample sizes are often too small to draw definitive conclusions (see Annex 8 for more details) the price sensitive consumers that appear to do best at avoiding higher priced platforms are those with the most financial knowledge, the most price aware and the most confident. However, there was no evidence that price sensitive consumers that search the most are more likely to select a lower priced platform than either non-price sensitive consumers or the population as a whole. This may reflect the complexity of searching, or it could be that even the most price sensitive consumers place more value on non-price criteria when making choices.

7.54 In summary, the evidence suggests that consumers who are relatively more price sensitive are only marginally more likely to select a lower priced platform than those who are relatively less price sensitive. Outcomes appear to be better for those consumers who are most knowledgeable and confident, but even for the most informed and engaged consumers, the probability of a price sensitive consumer choosing a low price platform is similar to that of other less price sensitive consumers.

Are financial indicators consistent with effective competition?

7.55 We looked at platform profitability which is a useful indicator of the competitive conditions in an industry. Widespread persistently high profitability across an industry is generally not consistent with a highly competitive market. We examined how revenues, costs and operating profit have evolved over time, and how they vary across firms, focusing on 20 of the largest firms based on AUA,[132] for the period from 2013 to 2016. Annex 4 sets out our analysis and findings in more detail.

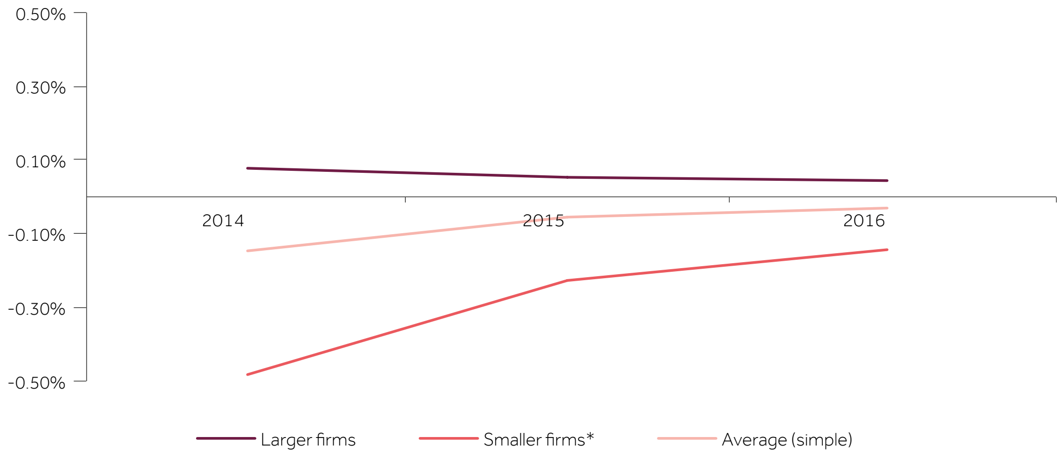
129 See appendix 8 for further details
130 Avoiding a higher price platform is equivalent to choosing a lower or medium priced platform.
131 Compared to the sample average and when compared to the least price sensitive consumers. The behaviours we considered included whether consumers searched for multiple platforms when choosing a platform, whether they used price comparison websites, whether they are confident about investing, their level of engagement and how aware they are of platform charges.
132 These firms represent approximately 90% of the platforms market by AUA.

Are platforms profitable?

7.56 We found a wide range of situations in terms of operating profit.[133] Across our sample of 20 investment platform firms, 8 firms had substantial positive contribution to operating profit over 2013-16. Another group of 7 firms had total costs significantly in excess of revenues. The remaining 5 firms posted an operating profit that was close or slightly above zero, indicating they break-even on operating expenses.

7.57 Trends in operating profit vary among firms. Figure 7.6 below shows operating profit per AUA, to adjust for scale. For 8 of the largest firms, operating profits were flat between 2013-16. For most of the others, operating profits improved over this period, from an initial situation of substantially negative profits, due to increased cost efficiencies. Not all firms that reported negative, below average profits were able to recover in the later years.

Figure 7.6: Operating profit/AUA over 2014-16



Source: FCA (2 outliers excluded within smaller firms). Please refer to Annex 4 for more detail

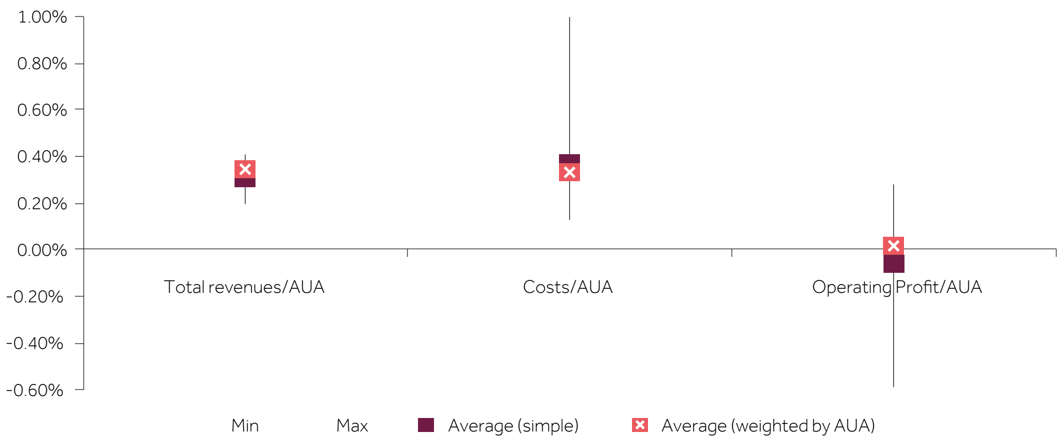
What drives financial performance?

7.58 We looked at whether variation in firms' operating profit is explained by differences in revenues or costs. Overall, as Figure 7.7 below shows, cost variation is much higher than revenue variation.[134] This implies that a firm's ability to control its cost base is a key driver of its financial performance.

133 Note that we have not been able to conduct a full profitability analysis by looking at return of capital employed or return on equity, since sufficiently granular data on firms' asset base is not available. However we believe that the economic cost of capital for the platform industry is relatively moderate, given that the investment platform business is relatively asset-light. As a result, we argue that operating profit is a useful indicator in this case to assess firms' financial performance.

134 Based on total revenues collected by firms, including from retail clients and institutional customers such as white-labelling, when applicable.

Figure 7.7: Variation in revenue, costs and operating profit across firms (2016)

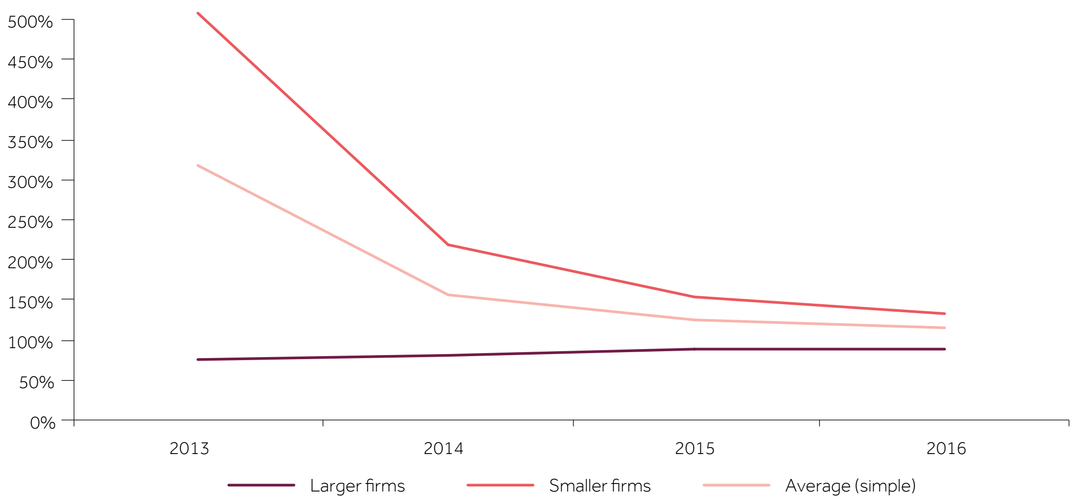


Source: FCA (2 outliers excluded in the metric revenues per AUA and operating profit per AUA. Please refer to Annex 4 for more details)

7.59 There was very strong revenue growth for firms in the platform market. 2013-16 revenues' Compound Annual Growth Rate (CAGR) was 35% on average for all firms,[135] and 18% using an average weighted by market share. This is consistent with the growth in AUA (40% and 24% respectively) and growth in customer numbers (32% and 18%).

7.60 Our sample of firms reported falling cost per AUA, suggesting that the industry is becoming more efficient. Costs remained flat for the largest firms, and decreased for smaller platforms, which can be explained by their different level of efficiency and the smaller firms catching up with the larger ones in terms of cost efficiency. This is reflected in Figure 7.8 which shows average cost-to-income ratio (CIR)[136] – a measure of efficiency – declining from 318% in 2013 to 115% in 2016. Smaller firms had not fully closed the efficiency gap by 2016. Cost allocation complexities for vertically-integrated players and the cost of large replatforming plans mean we interpret CIR figures with caution (see Annex 4 for details).

Figure 7.8: Cost-to-income ratio over 2013-16



Source: FCA

135 2013-2016 CAGR for all firms but 3, where we use 2014-16 CGAR due to data availability.

136 CIR captures whether a firm is able to cover its cost base through its various revenue streams.

Is there a relationship between financial performance and firm type?

7.61 We explored the relationship between financial performance, vertical integration and whether a firm has D2C or adviser platforms to understand if profitability differs between different types of firm. This helps us identify any differences in the competitive conditions in the market.

7.62 We found some differences between vertically integrated firms' and stand-alone firms' financial performance, particularly related to costs.

- On average, cost per AUA stood at 41bps for vertically integrated firms, compared to 27bps for stand-alone players in 2016.
- There was not much difference in revenues between vertically integrated firms and stand-alone investment platforms. On average, revenue per AUA stood at 32bps for vertically integrated firms (excluding 2 outliers), compared to 28bps for stand-alone firms (2016). There is no identifiable pattern in revenue growth – vertically integrated firms did not grow a higher rate than stand-alone firms (33% and 40% revenues CAGR 2013-16).
- Only 1 in 5 stand-alone platforms had negative operating margin in 2016, compared to 9 out of 15 vertically integrated firms. Vertically integrated firms tend to be less profitable than the standalone platforms.

7.63 Vertically integrated firms are able to cover their cost base through a wider pool of income, such as asset management and advice services. Our findings may reflect the challenges underpinning cost allocation for vertically integrated firms. As a result, we interpret this evidence with caution.

7.64 We did not observe any big differences in revenues, costs and operating profit per AUA between the D2C and the adviser segments (see Annex 4 for further details). Of the 3 firms that expressed a view on how the costs of running D2C and adviser platforms differ, 2 said adviser platforms tend to be more expensive to operate, and 1 platform argued the opposite.

Conclusions on platform financial analysis

7.65 There is a wide variation in profitability across the market. Variation in costs can be attributed to factors such as economies of scale,[137] the firm's maturity and operating efficiencies. As a result, this does not point towards a situation of sustained excess profitability on aggregate in this market.

7.66 We also saw a lower degree of variation in revenues per AUA compared to variation in costs per AUA. Thus, financial performance is primarily driven by a firm's cost base rather than its revenue levels. This is observed across the various business models, ie direct to consumer vs adviser segments, and stand-alone vs vertically integrated players.

137 Please see Chapter 8 for our discussion of economies of scale.

8 Barriers to entry and expansion

We examined whether there are barriers that may prevent competitors from entering or expanding in the platforms market. Platforms are often characterised as businesses that require scale, so we assessed whether there is evidence of economies of scale in the market.

Our analysis found a weak negative relationship between average costs and scale. However there are examples of small firms with low costs comparable to large firms, so scale may not be necessary as other factors can affect the cost base. We found no evidence that larger scale means lower technology costs.

It appears that firms with proprietary technology tend to have lower technology costs. New entrants, if they choose to outsource, can incur technology as a variable cost which facilitates entry. But costs do not necessarily fall as the firm expands. This may weaken incentives to expand compared to firms with proprietary technology.

Consumers tend not to shop around and switch platforms and many rely on brand when choosing a platform, suggesting that customer acquisition is likely to be a barrier to entry and expansion in the platforms market. This is supported by our analysis of marketing costs, where we find that larger platforms tend to spend proportionally more on marketing, and thus much more than smaller platforms in absolute terms. Marketing costs do not seem a significant barrier to entry, but smaller firms spending little on marketing may struggle to acquire customers and expand.

Regulatory costs are limited and do not appear to fall disproportionately on smaller firms. Firm responses to our data request did not raise specific regulations as a barrier to entry or expansion.

Introduction

8.1 Most platforms were established in the last 20 years with the onset of internet-based technology. We have seen relatively little entry in the platforms market in the last 5 years. The market shares among platforms have been relatively stable, but there has been entry and expansion by comparable firms such as asset managers, which increasingly distribute direct to consumers via a platform-like set up, and by firms offering online investment services such as automated advice.

8.2 There are 3 broad categories of barriers to entry or expansion: 'intrinsic' barriers, such as economies of scale, sunk costs, network effects and customer acquisition costs; strategic barriers, such as 'first mover' advantages and firm conduct; and regulatory barriers.[138] In this chapter we consider whether platforms face these types of barriers to entry or expansion.

138 Barriers to exit from the market can also act as a barrier to entry. As this was not raised as an issue in the platforms market we did not examine barriers to exit.

8.3 Platforms' technology is crucial for their business. We observed a mix of proprietary and outsourced technology. We aimed to understand whether technology outsourcing makes entry and expansion easier or harder.

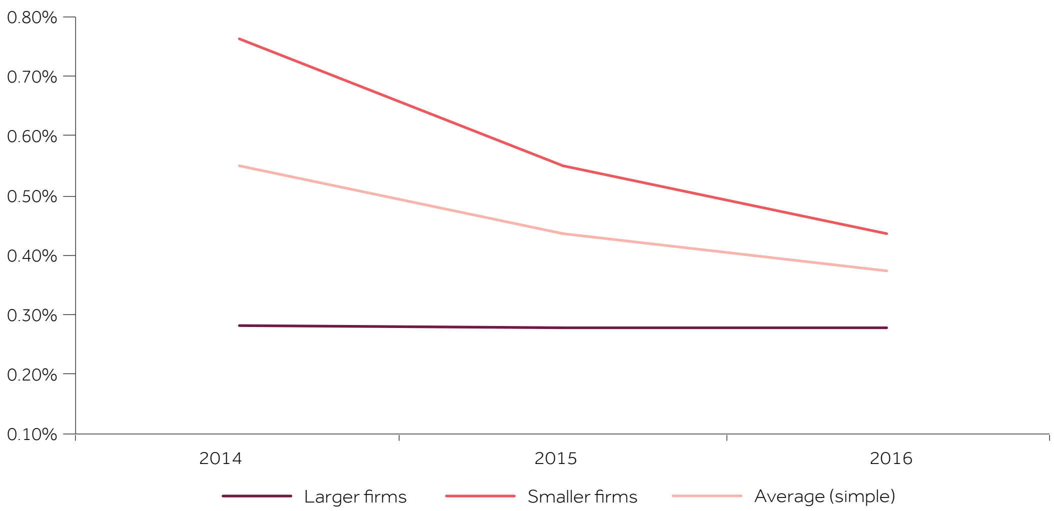
8.4 We consider whether difficulty in customer acquisition may prevent firms from entering or expanding in the market. We recap our findings on firm conduct and its implications for barriers to entry and expansion and consider whether regulation poses a barrier to entry or expansion.

Do investment platforms experience economies of scale?

8.5 We analysed firm financial data to understand whether there are economies of scale in the platforms market, that is, whether average costs fall as firms get bigger. Where economies of scale are significant, they can make entry or expansion on a small scale unprofitable. However, new entrants or challenger firms may still be able to enter the market and compete, for example, by aiming at a 'niche' in the market.

8.6 To assess the economies of scale, we examined how total costs vary with AUA, at firm level. Figure 8.1 suggests that, on average, there is a negative relationship between firm size and total costs. However, the underlying data also reveal that some smaller firms have low costs like some of the larger firms,[139] suggesting that a firm doesn't need scale for low average costs. Other factors may play a role. For example, the 3 smallest firms with the lowest costs are adviser platforms with relatively high average AUA per customer, and 2 of them also use proprietary technology.

Figure 8.1: Total cost relative to firm size over 2014-16



Note: Total costs per AUA over 2014-16. AUA calculated as average end-of-year AUA.
Source: FCA calculations based on firm data.

8.7 We also looked at the relationship between costs and scale for different cost categories. There are similar patterns for marketing costs, staff costs and compliance costs, indicating a negative relationship between these costs and scale. But many smaller firms have similarly low costs to the larger firms. The main economy of scale is staff costs. We observe falling staff costs per AUA as AUA increases. We did not see a negative

139 We do not show firm-level analysis so as to preserve the anonymity of firms.

relationship between technology costs and scale. There is some evidence to suggest firms benefit from a scale advantage to secure better interest rates on client cash.

8.8 There seems to be an element of economies of scale in the platforms market – we did observe a weak negative relationship between average costs and scale. But there are some examples of small firms with low costs comparable to large firms. This suggests that other factors increase the cost base, such as focusing on a relatively small number of wealthy customers or having proprietary technology (see below).

Does access to technology create barriers to entry or expansion?

8.9 We examined technology costs to understand whether they could act as a barrier to entry or expansion (see Annex 4 for further details of our analysis). Technology is the second most significant cost category to most firms after staff, representing around 15% of their overall costs in 2016.[140] This varies significantly as technology can represent up to half of the cost base for some firms.[141]

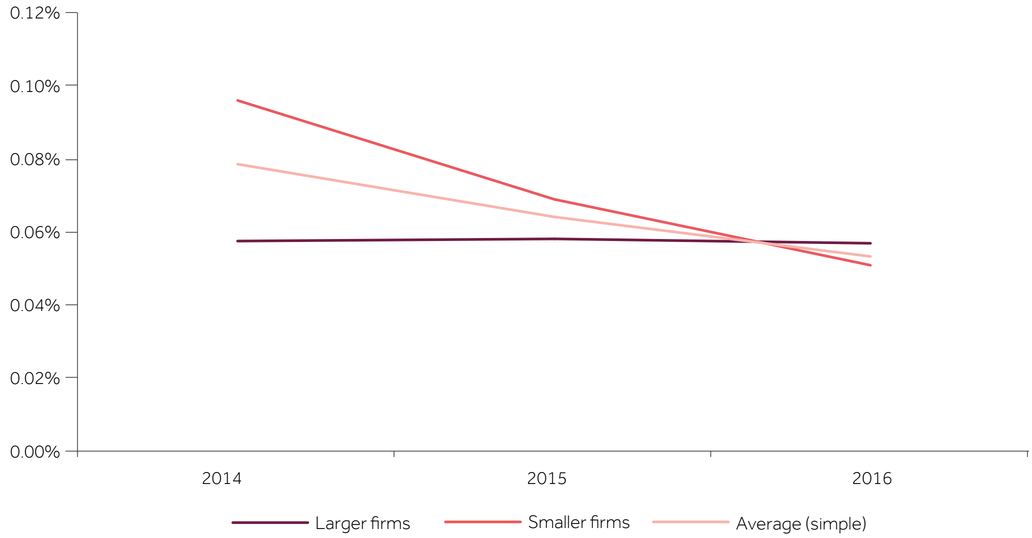
8.10 Most platforms outsource technology. Of the 38 firms for which we assessed technology strategies, 11 of them (6 of the top 20 firms) rely on proprietary technology for their platform business and the rest outsource technology either fully or partially. Adviser platforms outsource more than D2C platforms. We found that the average cost of technology across firms was 5bps of AUA, with most in the range from 2bps to 10bps. As Figure 8.2 shows, average technology cost across firms fell between 2014 and 2016. This is driven by smaller firms' falling technology costs, as larger firms' costs have been flat over the period.

8.11 There is no clear pattern on whether technology costs are lower for adviser or D2C platform firms, or vertically integrated or stand-alone firms. We did not find a clear link between technology costs and operating profit, though most of the profitable firms tend to have lower than average technology costs. Also, the age of a firm does not seem to affect technology costs.

140 This is based on self-reported costs. In particular, the allocation of staff –related expenses across technology, marketing and compliance can differ across firms.

141 Note that approximately half of the firms in our sample are currently or recently finished undergoing a replatforming exercise to move from older to newer technology. They are intended to improve efficiency and modernize the platform in line with latest market developments. In the absence of granular data, we are not able to distinguish between ongoing technology costs and non-recurring expenses attributable to replatforming. Such plans cover a multi-year period (typically 3 to 5 years), and are capital intensive (typically multi-million pound projects).

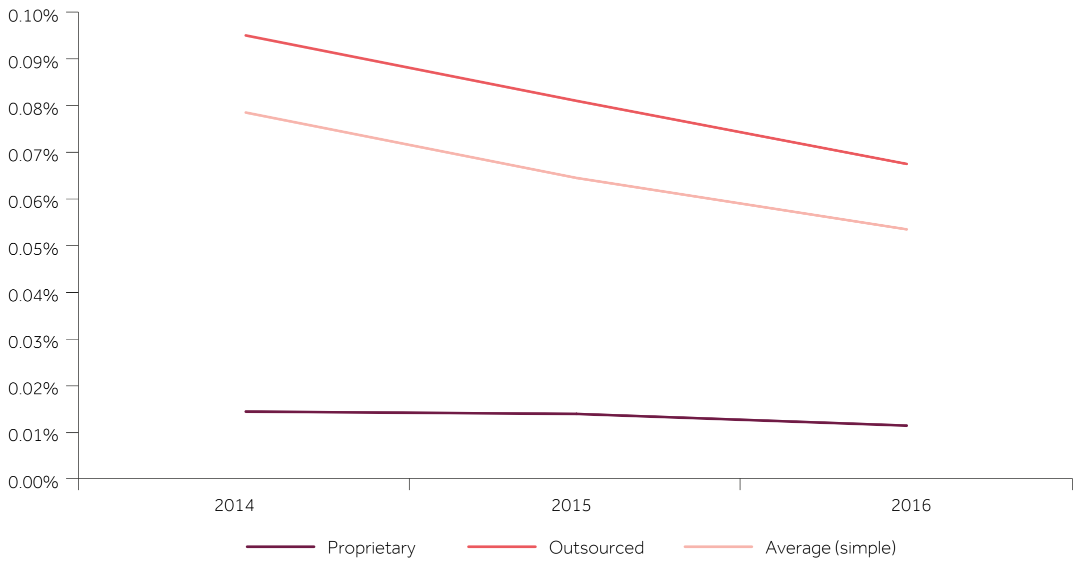
Figure 8.2: Technology cost over time



Source: FCA. Technology costs per AUA over 2014-16.

8.12 Although only a small number of firms in our sample have proprietary technology, they all seem to have lower technology costs than most of the platforms which outsource technology. This suggests that firms with proprietary platform technology may have a competitive advantage over those that outsource.

Figure 8.3: Technology cost by technology strategy



Source: FCA. Technology costs per AUA over 2014-16.

8.13 Our financial analysis suggests that, while firms may lower their technology costs over the longer run by investing in proprietary technology, technology outsourcing enables firms to incur the technology costs more like variable costs. Thus technology outsourcing can facilitate entry, but it could pose a disincentive or a barrier to expansion as the technology costs may not fall as much when firms grow, as compared to the firms with proprietary technology.

Do difficulties in customer acquisition create barriers to entry or expansion?

8.14 Chapter 3 showed there is limited shopping around for platforms and relatively low levels of switching, with many consumers relying on brand when choosing a platform. Some firms also cited brand as a barrier to customer acquisition and growth and customer acquisition more generally is seen as a barrier to expansion. We have seen an increasing trend for platforms to contribute to the payment of transfer fees to entice consumers to switch, which indicates barriers to switching can be barriers to customer acquisition. This suggests that customer acquisition is likely to be a barrier to entry or expansion.

8.15 We asked firms for estimates of their customer acquisition costs. They gave us a wide range, from £50 to £300 per customer, with rebates or financial incentives offered to win a new customer in the region of £150. Our estimates of marketing cost per new customer are of the same order of magnitude as the firms' estimates of customer acquisition costs.

8.16 Customer acquisition costs may also depend on whether a customer is new to the platforms market, or already uses another platform. Chapter 3 suggests that switching can be costly, time-consuming and complex, and it highlights that some consumers 'switch' by adding another platform, ie by 'multi-homing'. Multi-homing is common in this market which could be because firms successfully attract consumers despite their existing platform custom. There is a growing platforms market, and new customers may be easier to attract, as they are not subject to the switching process.

8.17 We examined firms' marketing spend to understand customer acquisition costs and whether smaller firms and entrants are likely to struggle. Average marketing cost for firms in our sample is 2bps of AUA, but there is significant variation across firms, with some spending next to nothing and a few spending in excess of 3bps of AUA.[142] However, financial data do not show convincing evidence that higher marketing spend results in higher revenue or customer growth or in better profitability, but our data may be too aggregated or too short (our time horizon is only 3-4 years) to spot any such trends.

8.18 Larger firms tend to spend more on marketing than smaller firms relative to AUA, although there are a few exceptions. If we consider marketing spend in absolute terms rather than relative to AUA, the spend of some larger firms is tens of times greater than that of the smaller firms. This suggests large firms have the scale and budget for marketing spend to enhance their brand and acquire more customers.

8.19 But the fact that there are many smaller and newer firms with relatively low marketing costs also suggests that small firms or new entrants may not need to spend more on marketing than the large incumbents in order to operate in the market. That is, customer acquisition and marketing costs may be more of a barrier to expansion than a barrier to entry.

8.20 Marketing cost varies by age and type of firm (whether adviser or direct or both), and there is no notable pattern between firms. However, we did find that vertically integrated firms have higher marketing spend than standalone firms. Yet there is no evidence to suggest causality for this observation.

142 Further details of this analysis are available in Annex 4 – Financial Analysis.

8.21 Overall, evidence from consumer research, firm responses and financial analysis suggests that difficulties in customer acquisition are a barrier to expansion.

Is regulation creating barriers to entry or expansion?

8.22 Some firms told us that the volume of regulation is a potential impediment to effective competition. The ability of firms to enter or expand in a market can be affected by the regulatory framework including through potentially sizeable compliance costs.

8.23 We examined firms' regulatory and compliance operating costs to understand whether they are a barrier to entry or expansion generally, or whether these costs fall on some firms more than on others. We found that:

- Compliance costs represent only around 2% of firms' costs on average[143] (with some small variations across firms) and stand on average at 1bp of AUA.
- Our analysis of compliance cost by firm size and firm type (ie advised platforms vs D2C platforms vs both, vertically integrated vs standalone) showed that these costs varied across firms without any obvious pattern. We did not see any evidence to explain why compliance costs are higher at some firms than others.

8.24 We asked firms whether they thought regulation acted as a barrier to entry, expansion or to good customer outcomes in the retail investment distribution market.

8.25 Firms that met the platform service provider definition did not say that they were at a competitive disadvantage when competing for investors with non-platform service providers (eg online portals restricted to the funds made by 1 asset manager that are not required to charge a separate platform fee) because of differences in regulation.

8.26 Firms did raise a number of issues that relate to the way regulation affects the provision of platform and ancillary services, which we set out below. A number of recent publications by the FCA have sought to address the issues they raised.

8.27 Some platforms were concerned that the FCA's descriptions of advice and guidance were unclear, and that this stopped them from helping customers with their individual situations. PS18/3, Perimeter guidance on personal recommendations on retail investments, provides the FCA's latest thinking on this issue and has a table of examples of what is and is not a personal recommendation and advice. Firms with questions on whether a service meets the definition of a personal recommendation are encouraged to contact the FCA's Advice Unit for clarification.

8.28 Firms stated that reduced bank appetite for short term deposits made it unsustainable to comply with existing client money regulations. PS18/2 has amended the 30-Day Rule to allow a firm to deposit an appropriate proportion of client money in an unbreakable deposit for up to 95 days, if certain conditions are met.

8.29 One firm said that seeking client consent to move them to a better position was difficult and detrimental to client outcomes. We think that this should be alleviated by

143 This is based on firms' self-reported compliance costs. However the allocation of staff–related expenses across technology, marketing and compliance can differ across firms.

the guidance which was recast in PS18/8 as FG18/3. This allows deemed consent to move consumers to cheaper share classes if they are better off as a result.

Conclusions on barriers to entry and expansion

8.30 The evidence suggests that there are not many barriers to entry in the platforms market, but there are some barriers to expansion. Difficulties in customer acquisition may be a barrier to expansion because:

- consumers face barriers to switching platforms
- most of the smaller platforms do not spend much on marketing compared to the larger incumbents.

8.31 There is some evidence of economies of scale in the platforms market, but taken together with firm profitability, this suggests that barriers to entry and expansion differ with business models. Firms aiming to enter and expand to achieve significant scale are likely to face more significant barriers than those that focus on a particular niche.

9 Areas for feedback and proposed remedies

In light of our findings, we are seeking feedback, considering further work and exploring potential remedies in 7 areas:

1. **Helping consumers on D2C platforms who find it difficult to shop around and choose platforms on the basis of price.** MiFID II has introduced total cost and charge disclosure requirements both before and after the point of sale, which should help improve comparability. Whilst we do not consider further costs and charges disclosure rules are required at this point, we will assess whether firms are using the MiFID II costs and charges disclosure requirements as an opportunity to innovate with different ways of providing costs and charges information to consumers. We will also explore whether there is scope for enhancing the role of third party intermediaries in helping consumers shop around.
2. **Strengthening the extent to which platforms drive competition between asset managers.** This includes exploring the positive and negative impact of commercial arrangements to secure the best or no worse fund price than are given to other platforms by asset managers. We will also assess how industry is innovating while complying with the costs and charges disclosures in MiFID II before considering introducing further remedies to improve the salience and comparability of fund charges.
3. **Helping consumers who may be building large cash balances and not taking costs into account in terms of the charges they pay, interest or investment returns foregone.** This includes ensuring that our existing rules go far enough in achieving our objective of consumers making informed decisions about the interest, charges and potential foregone investment returns on their cash balances.
4. **Making it easier for consumer and advisers to switch platforms.** This includes supporting the industry initiative to improve switching times and disclosure, and, in parallel, considering whether switching costs can be reduced through banning exit fees. As part of this work, we will look at the practical, policy and legal implications of such an approach. We will also look at improving switching between share classes and clarifying our expectations around charging for the adviser's role in switching.
5. **Making adviser platforms work better for orphan clients.** This could include requiring platforms to have a process to warn orphan clients that they should consider switching to a more appropriate proposition. We also intend to look at whether different charges levied on orphan clients (compared to non-orphan clients) are appropriate and, if not, whether we should tackle price discrimination between orphan and existing clients. We also intend to look at the merits of requiring platforms to determine whether a client has been actively using a firm's service and where this is not the case ensuring that any fees associated with the ongoing service are returned or the relevant service is provided.
6. **Helping consumers who may be exposed to risk levels they do not expect.** We propose to do further work to understand whether the issues we have identified are more broadly applicable to all types of model portfolios and to wealth and asset managers. Subject to that further work, we may look to introduce measures such as applying risk and performance disclosure obligations for funds onto model portfolios or requiring firms to use standard terminology to describe their strategy and asset allocation.

7. **Addressing potential non compliance with our rules.** We are seeking feedback on whether stakeholders consider our rules go far enough

We welcome feedback from stakeholders on these potential measures, and the work we propose to undertake to better understand the need for these potential measures, to help us further develop our final remedy package.

9.1 In this chapter, we set out the principles we use when considering potential remedies. We then set out the further work we will undertake and our early thinking on potential remedies to address the concerns we have identified.

9.2 This chapter contains our initial thinking on remedies for discussion. Our final report will set out the final package of proposed remedies to bring together a consistent and coherent set of measures. In doing so, we will take account of PRIIPs, MiFID II and the impact of related work, such as the AMMS, on this sector.

Key principles for considering remedies

9.3 As set out in our Mission, once we have identified a harm, and diagnosed its extent, causes, and how it may potentially develop, we have a range of options to explore when developing remedies.[144] These include rule-making powers and issuing guidance, supervision and enforcement action as well as giving the industry an opportunity to develop measures that ensure compliance and improve consumer outcomes. Any proposed rule-making remedies require consultation and an associated cost benefit analysis.

9.4 We want to identify proportionate and effective measures which address the concerns we have identified. When we propose remedies we consider:

- how the remedy addresses the interim findings and the harm we have identified
- the tools we can use, including issuing guidance or making new rules, our powers and our ability to make further rules, as well as constraints from relevant EU and domestic law on making new rules or issuing new guidance
- how the different remedies interact and work as a package to make competition work more effectively
- any potential costs and unintended consequences associated with the remedy
- how the remedy (or package of remedies) fit in with the FCA's other policies and actions relevant to platforms

Areas for feedback, further work and potential remedies

9.5 In this section we outline feedback we are seeking and our current thinking on the further work and potential remedies we could take forward to improve the way competition is working.

144 Available at: https://www.fca.org.uk/publication/corporate/our-mission-2017.pdf

Measures to help consumers on D2C platforms who find it difficult to shop around and choose platforms on the basis of price

9.6 As we outline in Chapter 5, we have found that consumers on D2C platforms may find it difficult to access and assess information about charges. This is because:

- many platforms charge a large number of fees and their pricing structures differ in terms of when a fee is incurred
- the level of the fee and the language used to describe otherwise similar fees is inconsistent
- pricing information is located in different places on a platform's website
- it can sometimes be difficult to find some price elements

9.7 If consumers' ability to access and assess charges information is limited, this makes it harder for them to select a platform that offers them value for money. If consumers cannot compare platforms, this limits the pressure on platforms to offer competitive deals.

9.8 Under MiFID II consumers should be given a single charge ex-ante in pounds and pence. While this will not include all the costs investors incur (such as exit charges), we think that this should simplify some of the complexity we have identified at the point of sale and help consumers to choose between platforms. As part of the Market Study, we did not assess whether firms are complying with the MiFID II costs and charges disclosure requirements. However, we will conduct a supervisory review to assess whether providers and distributors are providing the information required by MiFID II. We will reflect on the findings of our supervisory review to determine whether the difficulties consumers face when understanding and comparing the cost of a platform's services are due to non-compliance with MiFID II.[145]

9.9 The FCA's work on Smarter Consumer Communications,[146] as well as behavioural economics, suggests that the use of innovative practices in how information is provided to consumers, especially online, can have a significant impact on how well it is noticed and understood.[147] Some platforms provide investors with interactive tools to calculate the total charge based on their likely usage. We think that innovation like this would likely make the disclosure required by MiFID II more effective and help consumers understand what they are paying and help them better compare different platforms.

9.10 MiFID II came into force on 3 January 2018. Between the interim and final report we propose to assess how the industry is innovating as it implements the costs and charges disclosure requirements of MiFID II. After this, we will decide if more remedies are needed to help consumers compare costs and charges.

9.11 Third parties may also be able to play a greater role in helping consumers shop around and select a platform. In many other markets, intermediaries such as price comparison websites help consumers navigate complex price structures and reduce search costs by enabling them to compare products in one place. While platform consumers do not

145 COBS 2.2.1R and COBS 6.1.9R (for non-MiFID business) and COBS 2.2A.2R, 6.1ZA.11R and COBS 6.1ZA.12R (for MiFID business).
146 https://www.fca.org.uk/publications/discussion-papers/smarter-consumer-communications-further-step-journey
147 See for example Occasional Paper No. 32 Now you see it: drawing attention to charges in the asset management industry

currently use this sort of intermediary frequently, we welcome feedback on whether it would be beneficial for the FCA to introduce measures aimed at enhancing the role of intermediaries through:

- **Ensuring that platforms give intermediaries more data on platform cost and performance.** We could explore making it a requirement to provide information to help consumers select a platform.
- **Open data solutions** where consumers can export their usage history, including trading patterns, pot sizes and information about their funds, to third parties in order to make better decisions about the right platform for them.

Questions for feedback

Q1: Are you aware of specific innovations that display costs and charging information in a way which facilitates consumers making informed investment decisions?

Q2: Bearing in mind the existing costs and charges disclosure requirements[148] found in, for example, COBS 2.2.1R and COBS 6.1.9R (for non-MiFID business) and COBS 2.2A.2R, 6.1ZA.11R and COBS 6.1ZA.12R (for MiFID business), do you think additional disclosure remedies are required to ensure that consumers are able to compare platform charges? If yes, what should those further requirements be and why do existing disclosure requirements not go far enough?

Q3: Are there any practical challenges, negative effects or limitations of innovations to enhance the comparability of charges and, if so, are there ways in which these could be overcome?

Q4: Do you think that:

a. third party intermediaries currently face barriers to placing competitive pressure on platforms?

b. the role of third party intermediaries should be enhanced in an effort to improve competitive pressures on platforms and, if so, how?

c. a requirement on platforms to provide third party intermediaries with more data or open data solutions is a good way to enhance their role in an effort to increase competitive pressures on platforms?

d. there are practical challenges or negative effects of enhancing the role of third party intermediaries through introducing a

148 For example, COBS 2.2.1R and COBS 6.1.9R (for non-MiFID business) and COBS 2.2A.2R, 6.1ZA.11R and COBS 6.1ZA.12R (for MiFID business)

requirement on platforms to provide them with more data or open data solutions. If so, how could these be overcome?

Q5: **Are there any alternative ways to enhance the comparability of charges investors incur when investing through a platform?**

Strengthening the extent to which platforms drive competition between asset managers

9.12 We believe that platforms can help drive competition between asset managers. Our behavioural research suggests that by presenting fund charges information in a clear, understandable and prominent way, platforms and other intermediaries can increase the attention investors pay to charges.[149] This can drive greater competition between asset managers. Platforms may want to use the findings from our research when they design consumer journeys so that consumers can make informed choices between products. Between now and the publication of our final report we will assess how platforms are innovating in the way they are producing MiFID II compliance costs and charges disclosures.

9.13 In the context of this proposal, we will be looking at the extent to which disclosures are creating a clearer picture of the costs and charges associated with the funds that are available on the platform and whether the disclosure is helping to drive competition between asset managers. If we find that the disclosures (to consumers) are not helping to drive competition between asset managers then we will look at other ways in which we can improve the prominence and comparability of fund charges in a way which will help drive competition between asset managers.

9.14 As outlined in Chapter 6, platforms can play an important role in driving competition between asset managers. We found that a small number of large platforms have arrangements to secure the best or no worse fund prices than are given to other platforms by asset managers. The arrangements could reduce fund managers' incentives to make discounts available on other platforms. We welcome stakeholders' views on the positive and negative impact of such arrangements.

Questions for feedback

Q6: **Are you aware of specific innovations that display costs and charging information in a way which facilitates consumers making informed choices between investment funds?**

Q7: **Do you think additional disclosure remedies are required to ensure that consumers are able to compare fund charges on a platform? If yes, what should those further requirements be and why do existing disclosure requirements not go far enough?**

149 Occasional Paper No. 32 – available at: https://www.fca.org.uk/publications/occasional-papers/occasional-paper-no-32-now-you-see-it-drawing-attention-charges-asset-management-industry

Q8: Are there any practical challenges, negative effects or limitations of innovations to enhance the comparability of fund charges on a platform, if so, are there ways in which these could be overcome?

Q9: What impact do the commercial arrangements we have identified have on fund managers' incentives, on consumers and on competition?

Measures to help consumers who may be building large cash balances without knowing about interest, charges and potential lost investment returns

9.15 As we outline in Chapter 5, we found that some investors on D2C platforms accrue large cash balances. Our analysis of firms' data shows that in 2017, there was £16bn held in cash on D2C platforms, which is 8.8% of AUA on D2C platforms.[150] By comparison, we found that cash accounted for 3.8% of AUA on adviser platforms.[151]

9.16 This gives rise to 2 potential concerns. First, consumers may be mistakenly holding cash balances instead of investing their cash balance to build greater returns. Second, the relatively high cash balances might suggest the cost of holding cash is not transparent to the consumer. If the interest that platforms pay and the charges they levy on cash are not easy to find and compare, consumers are unlikely to take this into account when choosing a platform, reducing the pressure on platforms to offer competitive interest rates.

9.17 CASS 7.11.32R requires firms to pay a retail client interest earned on client money held for that client unless it has otherwise notified the client in writing. Firms are also required to disclose the costs and charges information associated with the platform service, ie for holding a cash balance.[152] Further, COBS 6.1E.1R requires a platform service provider to clearly disclose the total platform charge to a retail client before providing the client with any services.

9.18 We believe that a combination of these existing rules should work to ensure that consumers are getting relevant information about the costs associated with holding cash balances and any interest that may be payable on such balances. However, the fact that a relatively high proportion of consumers are holding cash balances could suggest these rules may not be having their intended effect and we are keen to better understand why this may be the case.

9.19 To address these concerns we want to better understand why consumers are building large cash balances and whether existing rules on disclosure go far enough or whether further rules and/or guidance is required[153] to ensure our policy objective – to ensure consumers are making informed decisions – is achieved.

9.20 We are also aware that some platforms charge platform fees for consumers who hold cash on the platform. We would like feedback on the reasons why platforms do so and whether consumers are aware of these charges.

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150 Figures are for June 2017.

151 For 2017, of the D2C firms in our sample that provided data, £45m was held in cash ISAs compared to £162 billion in stocks and shares ISAs and £27bn held in cash outside cash ISAs.

152 See COBS 2.2.1R and COBS 6.1.9R (for non-MiFID business) and COBS 2.2A.2R, 6.1ZA.11R and COBS 6.1ZA.12R (for MiFID business)

153 For example, rules in place for SIPPS require cash interest payments to be included in projections. See also https://www.handbook.fca.org.uk/handbook/COBS/13/Annex3.html#D213

Questions for feedback

Q10: **What are the reasons why D2C consumers have significantly higher cash balances than advised consumers?**

Q11: **How are cash balances held, ie does it tend to be in a wrapper or for certain products, and how long does it stay uninvested for?**

Q12: **Are certain types of consumers more likely than others to hold large cash balances and, if so, why?**

Q13: **What determines how the level of interest rates on cash balances paid to customers is set?**

Q14: **What reasons are there for platforms to charge a platform fee on cash and what are the costs for a platform associated with holding consumers' cash?**

Q15: **How much cash should consumers reasonably hold, and for how long?**

Q16: **As set out in paragraph 9.18 there are a number of existing rules which require platforms to disclose information that is relevant to a consumer holding a cash balance. Given the high proportion of cash balances:**

a. **how could the relevant disclosure requirements be made more effective at warning consumers of the costs and charges associated with holding cash balances?**

b. **do you think there are better alternative options which could make consumers aware they are holding cash balances and the charges associated with doing so?**

Measures to make it easier for investors and advisers to switch platforms

9.21 As discussed in Chapters 3 and 4, the switching process for investors and advisers is complex and time consuming. We identified a small but significant group of consumers who tried to switch platforms but had been put off by the difficulties they faced in doing so. We are concerned that this might result in consumers staying on platforms which no longer meet their needs or fail to offer them value for money. Over time, this may also result in there being less competitive pressure on platforms.

9.22 We recognise that there are industry-led attempts to make the process more transparent and establish minimum standards on switching times and processes. Following discussions with Supervision, in February 2016 a number of trade associations established the Transfers and Re-registration Industry Group (TRIG) to establish best practice on switching, including through platforms. We expect this to provide:

- **a minimum standard for transfer and re-registration times** through the introduction of a maximum timescale for each step in the switching process

- **clear customer communications** from the recipient provider at the outset of the switching process detailing the transfer process, timelines and a point of contact if they have any questions or wish to complain

9.23 We welcome views on whether and how the FCA can reinforce the industry initiative. We are interested to hear views on what that role could be and how it should build on the industry initiative. One way we could do this is to implement a requirement on platforms to provide a prompt and efficient service to enable a retail client to move to another platform.[154] We could support such a requirement with Handbook guidance that sets out the FCA's expectation in relation to what a 'prompt and efficient' service might look like in relation to platforms. The guidance might be informed by the minimum standards for transfers developed by industry for the purpose of complying with the re-registration requirements of retail investment products in COBS 6.1G.1R.[155]

9.24 A further positive step would be for industry to **publish data on transfer times** so consumers and third parties can compare platform performance and incentivise platforms to make improvements.

9.25 We expect the industry to implement changes in these 3 areas by the time we publish our final report in the first quarter of 2019. If we are not satisfied with the progress that has been made by that point we will consider the merits of further FCA action in this area. This could include introducing so-called "sunlight remedies", whereby firms or the FCA would collect and publish data on transfer times completed by different parties in the transfer process in order to draw consumers' and third parties' attention to differences in the time it takes for different firms to switch customers. A more radical approach would be for the FCA to set minimum standards for transfer times.

9.26 These measures are designed to improve the overall switching process and timeframes, but there are several costs consumers can face when switching platform. Therefore, as well as finding ways to facilitate a smoother switching process, we are considering whether to introduce additional remedies to reduce the charges some platforms levy on clients wishing to switch.

9.27 The options we would like feedback on are:

A: Banning Exit Fees

9.28 We are considering preventing platforms from charging platform exit fees. As part of this we intend to further examine the practical, policy and legal considerations which either support or undermine this proposal. As outlined in Chapter 3, consumers cite exit fees as one of the top 3 actual or perceived barriers to switching although we note that not all platforms charge exit fees. There may be some legitimate costs associated with transferring consumers, and we welcome views on the likely impact of this potential remedy on platforms' business models and alternative ways they may seek to recover any such costs if a ban on exit fees were introduced. Consumers may also incur product and wrapper exit fees if they switch both platform and their underlying investments. We welcome views on what the scope of any ban on exit fees would need to be to achieve its intended aim of reducing barriers to switching.

154 Such a requirement could, for example, be modelling on the retail banking switching requirement that can be found in BCOBS 5.1.5R.

155 This rule requires re-registration requests have to be made 'within a reasonable time and in an efficient manner' as required by COBS 6.1G.

B: Providing further guidance around our expectations for adviser charges for switching

9.29 We are considering whether we should clarify our expectations for advisers that are charging their clients for switching platforms through guidance. As outlined in Chapter 4, we found that a significant number of advisers said that they would likely charge clients an extra fee for switching platform on top of their ongoing adviser fee. Advisers who did so told us that this was because a platform switch was an advice event which required the production of a suitability report.

9.30 We recognise that it may be reasonable for advisers to charge for services associated with switching platform. However, it is not clear to us why meeting suitability requirements to switch platforms should outweigh the benefits of switching. This is particularly the case where a firm already offers some form of ongoing suitability assessment and should therefore already have up to date information about the client's circumstances and objectives, and where advisers regularly undertake due diligence on the platform market.

9.31 We welcome views from stakeholders on exactly what additional work is required to meet suitability requirements over and above the ongoing suitability assessment and how such additional work translates into the level of fees being charged to help a client switch to another platform beyond ongoing advice charges.

C: Measures which would improve switching between share classes

9.32 As outlined in Chapter 3, it can be difficult to undertake re-registration transfers for investors who are in share classes which have been created specifically for a particular platform (typically because the platform negotiated a discount). To make this process easier we could require the ceding platform to first transfer the consumer to the gaining platform's share class before the switch takes place. There is at least 1 platform which currently does this.

Questions for feedback

Q17: Is there a role for the FCA in reinforcing the industry initative to improve transfer times and, if so, what should this role be?

Q18: What is the likely effectiveness and proportionality of:

- **a. The possible remedies outlined in this section which are intended to make switching easier and increase the competitive pressures operating in the platform market?**
- **b. FCA measures that are intended to improve the switching times and processes by, for example, introducing remedies to shine a light on firms' switching times or setting minimum standards for transfer times?**

Q19: What should be the scope of a remedy to ban exit fees (ie should the ban apply to platofrm fees only, or also eg product-specific fees)?

Q20: Would there be any unintended consequences associated with any of the possible remedies outlined in this section which aim to make switching easier? If so, how could these be overcome?

Q21: What costs do advisers incur when reviewing whether they should switch their clients to an alternative platform and then executing a switch?

Q22: Would guidance on our expectations for adviser switching be useful? If so, what do you think this should cover? If not, what alternative remedies could achieve our aim of ensuring the costs of swtiching adviser platform are proportionate?

Measures to help orphan clients

9.33 We found that there are currently just over 400,000 orphan customers with over £10bn of assets on platforms, and that this figure has been rising. These customers are often subject to extra charges, face unreasonable barriers to trading or have a reduced ability to access funds. We estimate that at least 10,000 customers are paying penalty fees of over £1.2m a year. In order to address these issues, we want to explore a number of potential measures:

- **A: Tackling price discrimination between orphan and existing clients.** A number of platforms impose extra fees on orphan customers and these extra fees appear excessive compared to any additional administration cost associated with these orphan customers. We want to hear persuasive explanation as to why orphan customers are being charged more. In the absence of persuasive explanation, we will explore whether remedies which ensure orphaned clients are aware of the higher charges they pay or prevent platforms from charging orphan clients more than existing clients would deliver better outcomes for orphaned clients. In doing do, we will explore which remedies are practically and legally viable.

- **B: Requiring platforms to have a process in place to get orphan customers to switch to a more appropriate proposition.** Orphan customers are unlikely to be well served by staying on adviser platforms as their ability to access and alter their investments is typically highly restricted. We have found that a minority of platforms do not have an orphan customer process. We believe that platforms could do more to get orphan clients to find a new adviser or switch to a D2C platform and are considering whether existing rules (such as acting in the client's best interests[156]) should be used to achieve this policy objective or whether new rules might be required.

- **C: Requiring platforms to check if there is no activity after a year to ensure their customers are receiving an advice service.** Clients can be effectively orphaned if they are paying for an ongoing advice service that their adviser is not providing. With 1 exception, we found that platforms do not proactively monitor whether there has been activity on accounts where the customer pays an ongoing advice charge. We are seeking feedback on whether it is necessary to amend our rules (eg COBS 6.1B.9R) so that platforms are required to periodically check whether a retail client's

156 See COBS 2.1.1R

existing instruction remains valid and to inform the FCA of orphan clients who are still paying an adviser for ongoing advice.

Questions for feedback

Q23: **What is the likely effectiveness, proportionality and unintended consquences of the remedies listed above (A-C)?**

Q24: **Should remedies A-C apply to orphan clients only or other groups of consumers?**

Q25: **Would platforms face any practical challenges in introducing remedies A-C above?**

Measures to help consumers who may be exposed to unexpected risk levels

9.34 As we discuss in Chapter 6, 17% of non-advised consumers use ready-made model portfolios. Such consumers are typically less active users of platforms, younger and less affluent. There has been steady growth in the model portfolios offered by platforms, with AUA in in-house model portfolios increasing from £5bn in 2011 to £37bn in 2017, with similar products also being offered by wealth and asset managers.

9.35 Our findings show that it is very difficult to compare similarly labelled in-house model portfolios due to limited consistency between platforms in risk labels and descriptions. We think it is important for consumers and advisers to make an informed choice about model portfolios and select products which offer consumers their desired level of risk exposure.

9.36 To follow up from our work so far, we plan to do further analysis in 2 areas. First, we would like to understand whether consumers or their advisers would be able to assess the risk levels of portfolios without the naming conventions, such as 'cautious', 'adventurous' and 'balanced'. Second, given the wide range of charges, the next step is to identify the main drivers of the difference in charges for model portfolios by platforms and comparable firms.

9.37 We also plan to do further work between the interim and final report to explore whether the issues we have identified with in-house model portfolios might apply more broadly to all types of model portfolios and to equivalent products offered by wealth and asset managers. Depending on what we find, we may then explore introducing remedies to address these concerns. These potential remedies could include:

- applying current performance and risk disclosure obligations for funds onto model portfolios
- requiring firms to use standardised terminology to describe their strategy and asset allocation, including formalising definitions such as cautious, balanced and adventurous

Questions for feedback

Q26: **We welcome views on whether the issues we have identified with in-house model portfolios are likely to apply across all types of model portfolios and also exist in model portfolios offered by wealth or asset managers.**

Q27: **What is the likely effectiveness, proportionality and unintended consquences of the remedies that would:**

a. apply current performance and risk disclosure obligations for funds onto model portfolios?

b. require firms to use standardised terminology to describe their strategy and asset allocation, including formalising definitions such as cautious, balanced and adventurous?

Addressing potential non-compliance with our rules

9.38 As we discuss in Chapter 4, we found that advised platforms mostly compete to offer services that provide benefits to consumers. We have observed that some platforms supply services which might alter an adviser's incentives, without considering whether the provision or receipt of these services might constitute a non-monetary benefit which needs to comply with our inducement rules. These services include education and training, white labelling customer portals and some software tools.

9.39 Both platforms and financial advisers should consider whether the non-monetary benefits they offer or receive, such as training and white-labelling facilities, are compliant with applicable Handbook rules, for example COBS 2.3. (for non-MiFID business) and COBS 2.3A (for MiFID business).

9.40 As we discuss in Chapter 6, we have found that investment platforms who provide stockbroking services to retail investors could do more to ensure consistent compliance with their best execution obligations. In general terms, the best execution requirements require firms that are executing client orders to:[157]

- establish and maintain such execution arrangements and execution policy that allow them to consistently obtain the best possible results for their clients
- provide information on their execution policy to clients
- obtain prior consent of its clients to their execution policy
- provide information on where an order was executed
- monitor the effectiveness of their execution arrangements and policy
- conduct regular reviews of their execution arrangements and policies
- be capable of demonstrating that they have executed orders in accordance with their execution policy

157 The FCA's requirements on best execution also apply to portfolio managers and firms who receive and transmit orders with other entities for execution. See COBS 11.2A (Best execution – MiFID provisions)

- publish information annually of the top 5 venues they have used to execute client orders

9.41 We consider that our rules in this area are sufficient and that firms complying with our rules will provide retail investors with the information they need about how their orders will be executed by the firm. However, we welcome feedback on this.

Questions for feedback

Q28: **To what extent do existing rules go far enough in making platforms' trading practices transparent to retail investors?**

Abbreviations used in this paper

AMMS	Asset Management Market Study
AR	Appointed Representative
AUA	Assets Under Administration
bps	Basis points
CAGR	Compound Annual Growth Rate
CASS	Client Assets Sourcebook
CGT	Capital Gains Tax
CIP	Centralised Investment Proposition
COBS	Conduct of business sourcebook
CPD	Continuing Professional Development
D2C	Direct to consumer
DFM	Discretionary Fund Manager
EA 02	Enterprise Act 2002
FA	Financial Adviser
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
GIA	General Investment Account
ISA	Individual Savings Account
MiFID	Markets in Financial Instruments Directive
OCF	Ongoing charges figure
PRIIPs	Packaged Retail Insurance-based Investment Products
RDR	Retail Distribution Review
RFI	Request for Information

RSP	Retail Service Provider
SIPP	Self Invested Personal Pension
VI	Vertically Integrated

We have developed this work in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

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FINANCIAL
CONDUCT
AUTHORITY

12 Endeavour Square London E20 1JN
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk