

Annex 2

Regulatory boundary of generic financial advice

2.1 The attached paper *Review of the Advice Boundary* by a consultant to the Review team, Nick Lord, reviews the scope of generic financial advice (GFA) and its boundary with regulated financial advice in light of the prototype experience. It also responds to regulatory issues raised by respondents to the Review's Interim Report and observers of the prototype services.

2.2 The paper concludes that advice protocols can be developed which contain GFA outside of FSA and Consumer Credit regulation. It also suggests how a GFA service, with appropriately trained advisers can fully utilise the scope within which GFA can operate and remain distinct from regulated financial advice.

2.3 The Review's response to the advice contained in the paper can be found in Chapter Three.

Review of the Advice Boundary of the Prototype Services

1. Introduction

1.1 Annex 4 of the Thoresen Review's Interim Report¹ analysed the factors that determine the boundary between generic and regulated financial advice. As the annex explains, this complex matter involves consideration of the Financial Services and Markets Act 2000 (FSMA), the Consumer Credit Act 2006 and other legislation. Furthermore, in some aspects of generic financial advice (GFA), such as guidance on choice of utility provider, there is no regulation that prescribes the advice boundary, although there are overriding legal and professional indemnity constraints.

1.2 The Interim Report established a working definition for the parameters of GFA that was implemented in the prototype GFA services. It is important to note that the review team did not use regulation as the sole benchmark to establish the advice boundary for the prototype services. Rather, they set an advice boundary that provided a consistent approach across all financial products and provided clear differentiation with regulated advice.

1.3 The regulatory boundary is obviously an important factor in the delivery of GFA. Before the prototypes, it was unclear whether it would be possible to provide GFA without straying into regulated financial advice. If it were possible to provide guidance without crossing this line, it was uncertain whether it would be worthwhile and prompt people to take action. This paper therefore reviews the scope of GFA and its boundary with regulated advice in light of the prototype experience. It also responds to the regulatory issues raised by respondents to the Review's Interim Report.

1.4 The paper briefly confirms the factors that determined the prototype advice boundary and then discusses:

- the impact of the advice boundary on the scope of GFA provided in the prototype services;
- two additional regulatory issues raised in response to the Interim Report.

2. The factors that determined the prototype advice boundary

2.1 The Review's Interim Report provided a working definition of the parameters of GFA as follows:

- **GFA will** provide information and guidance to people on a range of financial topics, dealing with each topic to a consistent level of depth. It will translate financial jargon and equip people with questions to ask of providers.
- **GFA will** provide guidance on a suggested course of action. For example, it will suggest to a new parent "most people in your situation

¹ http://www.hm-treasury.gov.uk/media/9/6/thoresenreview_annex4.pdf

consider life cover". It will then provide information on the pros and cons of different types of protection and the consequences of not holding insurance then guide users towards appropriate comparison tables and/or signpost them to the regulated advice sector.

- **GFA will** signpost individuals to other services in the financial services sector, government or the third sector depending on the needs of the individual.
- **GFA will not** make recommendations to buy, surrender or change a specific product from a specific provider.
- **GFA will not** provide in-depth information or guidance on complex debt, tax or benefit cases. It will provide budgeting guidance and signpost individuals to specialist agencies.

2.2 The prototype services used advice protocols as the basis for implementing these parameters. The prototypes were established within a short timescale and aimed to test the effectiveness of advice from both skilled and less skilled advisers². Consequently, the advice protocols were worded very tightly. In addition to prohibiting recommendations for products from specific *providers*, the protocols also directed advisers away from making any explicit recommendations, which would have included recommending a type of product. The protocols prescribed that advisers could explain about the different types of products and the advantages, disadvantages and implications of each type, but they could not provide recommendations. They could say, for example, that "most people in your situation would be well advised to consider life insurance", but they should not go as far as saying "I recommend life insurance to you".

2.3 It should also be noted that to implement the principle of providing guidance to a consistent level of depth, the prototype services defined "financial product" to include the full range of financial products and services and not only those normally covered by the mainstream financial services sector. Hence, the restriction on explicit recommendations applied to non-regulated products such as utilities as much as to regulated products. Annex 4 of the Interim Report provides more detail on the complex regulatory issues that helped inform the Review's approach to the boundary of the prototype GFA services.

3. The impact of the advice boundary on the scope of GFA provided in the prototype services – the adviser perspective

3.1 Feedback from the prototype advisers indicates that they were initially concerned about the advice boundary. The extent of their concern varied according to their experience in providing guidance on financial issues.

² Skilled advisers had experience of working in the financial services industry but were not fully qualified regulated advisers. For example, one skilled adviser was CeMap qualified with 5+ years experience of working in the pensions industry. Less skilled advisers had customer-handling experience from working in either call centres or the retail sector.

3.2 The more experienced advisers feared that the boundary would unduly limit their ability to offer advice on specific products already held by clients, even where (for example in the case of high-interest credit card debt or an expensive utility provider) the adviser was used to recommending that the client should change their product.

3.3 These advisers reported that their concern about the advice boundary eased as the prototype services progressed and they realised that the scope of GFA offered ample opportunity for assisting their clients. Advisers' concerns also reduced as they saw that some of the client questions were relatively basic and unconnected with financial products, and therefore did not require consideration of the boundary of GFA.

3.4 Where clients did want advice on specific products, advisers generally felt comfortable explaining that they could not provide such guidance and then further explaining where guidance was available. In a small minority of cases, advisers were concerned that they were not able to meet the client's need for a product recommendation.

3.5 The less experienced advisers and those responsible for writing training materials understandably focused on the need not to overstep the advice boundary. It seems likely that this, at least to some extent, diverted their attention from the very positive assistance that they could still provide within the scope of the prototype services. Additionally, low call volumes and limited training meant that advisers did not gain the necessary confidence and technical knowledge to utilise the full depth of GFA.

3.6 Overall, there is no evidence from the prototype services that, from the point of view of the advisers, the advice boundary restricted the advisers' ability to assist their clients. However, the evidence is less clear about how far the boundary would affect a future GFA service if it were to use more experienced advisers who are confident at utilising the full extent of GFA. It seems very possible that larger scale testing with increased volumes and a different mix of advisers could result in a service that more seriously tests the boundary between generic advice and regulated advice.

4. The impact of the advice boundary on the scope of GFA provided in the prototype services – the client perspective

4.1 Evidence from the independent evaluation of the prototype services³ shows that a high proportion of clients said that they were helped by the advice from the prototype service they used. Eight out of ten clients took at least one form of action within a week or so of using one of the prototype services. In addition, of these, one in four had a discussion with a supplier of a new financial product. This provides indicative evidence that maintaining a

³ Annex 1, *GFA Prototype Evaluation, Research Report for the Thoresen Review* by Andrew Smith and Midge Clayton.

clear boundary with regulated advice did not prevent clients from taking action.

4.2 However, it is unclear whether extending GFA closer to the regulatory boundary would have been even more helpful. Analysis of the views of some users of the prototype services⁴ shows that there was a demand for more product-specific advice. The same research shows that around half the people more generally surveyed agreed strongly with the idea that a GFA service “should be able to recommend the best product for me”.

5. The impact of the advice boundary on the scope of GFA provided in the prototype services – stakeholder feedback

5.1 Most of the industry stakeholders who listened to recorded telephone calls to the prototype services and/or visited the prototypes also felt that the boundary with regulated advice did not restrict the advice provided by the prototype services.

5.2 Some industry stakeholders were concerned that prototype advisers had occasionally stepped over the boundary into regulated advice by, for example, suggesting that a client should take out a particular type of mortgage (but without any discussion of a specific provider).

5.3 In one case, an adviser suggested that a fixed-rate mortgage seemed the best option for the client’s circumstances as a first-time buyer. This advice went beyond that prescribed by the protocols because it was an explicit recommendation as opposed to laying out the options. However, it was still unregulated advice because it did not relate to a specific regulated mortgage contract. This demonstrates the confusion that exists in many stakeholders’ minds around what GFA can actually provide without crossing the regulatory boundary.

5.4 As set out in Annex 4 of the Interim Report, this confusion is understandable. Recommending types of products requires a GFA service to make risk-based judgments and carefully navigate regulation, which treats existing product holdings differently from new products. For example, recommending that a first-time buyer consider a fixed-rate mortgage (but without mention of a specific product provider) is not treated as regulated financial advice. However, recommending that a current mortgage holder switches to a fixed-rate mortgage (again without mention of a specific product provider) is regulated financial advice. This is likely to be confusing for both clients and advisers. It would also conflict with the Review’s principle of a service that provides a consistent level of guidance.

5.5 It is evident that a future GFA service will need more clarity about what advisers can and cannot say without breaching regulation. In February 2008,

⁴ Annex 1, *GFA Prototype Evaluation, Research Report for the Thoresen Review* by Andrew Smith and Midge Clayton.

the FSA produced a factsheet on what advisers could discuss around money matters without FSA authorisation. This is a useful start at clarifying the regulatory boundary. It would, however, be helpful if the FSA could expand on the guidance and provide practical assistance to future providers of GFA and consider how their guidance could include non-FSA regulated matters.

5.6 As Annex 4 to the Interim Report makes clear, the regulatory boundary is not only a matter for the FSA. GFA covers a wide range of financial issues and advisers will need clarity across this range.

6. Specific regulatory issues raised by stakeholder comments – the Compensation Act 2006

6.1 Stakeholder response to the Interim Report has raised the possibility that a GFA service may need authorisation under the Compensation Act 2006. The concern here is that the GFA service might advise a client of a potential complaint against their financial services provider. This could fall within the reach of the Act because the regulation covers claims made against financial products and services. Article 4 (2)(b) of the Compensation (Regulated Claims Management Services) Order 2007 provides that “advising a claimant or potential claimant in relation to his claim or cause of action” constitutes a regulated activity.

6.2 The prototype services did not charge users for its advice and nor did it receive any payment from any third party to whom it referred its clients. In the case of complaints against financial services providers, the advice protocols only referred to the role of the Financial Ombudsman Service. Under these constraints, the opinion of those responsible for administering the claims management regulations is that the prototype GFA service was not required to seek authorisation.

6.3 Future authorisation would be required if a GFA service were to negotiate a commission or other payment when referring clients to solicitors or claims management companies for further advice about a complaint. Future testing of a GFA service should bear this in mind. However, such a payment arrangement seems unlikely to fit with the principles of any not-for-profit GFA service.

7. Specific regulatory issues raised by stakeholder comments – comparison websites and financial promotions

7.1 The prototype advice protocols suggested that comparison websites offer one option for consumers to compare financial products. The common advice protocol proposed that the prototype services should explain about the availability and potential usefulness of such website, but it should also explain the weaknesses. For example, the sites may not be whole of market and, with the exception of the FSA comparison website, all sites receive income from

“click-throughs”, which should be borne in mind when relying on the product rankings, recommendations, or “best buys” offered by these websites.

7.2 Some stakeholders who listened to prototype calls to a prototype service were concerned that advisers might be making a financial promotion when referring clients to a comparison website and, that in so doing, the advisers were providing regulated advice.

7.3 Again, the regulatory boundary is unclear. In suggesting that a client refers to a comparison website, the generic adviser is arguably making an introduction to that website. After consulting the website, the client may subsequently buy a regulated product. The question then becomes whether in making the introduction, the adviser is making an invitation or inducement for the client to take out a specific regulated agreement. If the adviser makes such an invitation or inducement, then he or she makes a financial promotion and, unless otherwise exempt from regulation, breaches the regulatory boundary.

7.4 The FSA Perimeter Guidance manual sets out at PERG 8.4.22G that “an introduction may be an inducement if the introducer is actively seeking to persuade or incite the person he is introducing to do business with the person to whom the introduction is made”. Whether the GFA adviser will meet this test could depend on how and why the adviser suggests that the client identifies and uses the comparison website. There is a difference between a generic adviser simply providing information about how comparison websites are a potentially useful tool for consumers (e.g. “Here is a list of some websites where you might find useful information about a range of types of products that we discussed”) and a specific steer towards a comparison table to meet a specifically identified need (e.g. “As a single parent with young children, it is important that you prioritise life insurance; here is a website where you can find out how much individual providers charge for such insurance”).

7.5 Many stakeholders have stressed how important it is that generic advice encourages clients to take financial action. They argue that where it is generally agreed that a specific financial approach is appropriate (e.g. those with dependants should take out life insurance, or those in debt should prioritise debt repayment after accumulating an appropriate level of “emergency” savings), the generic adviser can encourage such action by referring clients to further appropriate sources of information and advice which may lead to the purchase of a specific product. In such situations, it seems likely that the GFA adviser is making an inducement in referring a client to a comparison website.

7.6 However, informal legal opinion has advised that a specific referral to a comparative website *may not* be the problem envisaged by some stakeholders. Even if the generic adviser does induce the client to visit the comparison service website for the purpose of entering into an agreement for the provision of advice or arranging services or to buy an investment, it is highly probable that there is an exemption for one-off non-real time or solicited

real time communications in article 28 of the Financial Promotions Order. This would be on the basis that the financial promotion is made in the context of the generic advice given to the consumer, which will have been tailored to their individual circumstances.

7.7 However, this is just an informal interpretation of the perimeter guidance and there must therefore still be some element of doubt about whether this is a potential future issue for further testing of the GFA service. Again, more guidance in this area from the FSA is important for future testing of the GFA service.

8. Specific regulatory issues raised by stakeholder comments – how can a GFA service identify an appropriate comparison website provider?

8.1 Even if referral to a comparison website is not a regulatory problem, there remains a problem for a future GFA service in knowing which websites can be trusted to offer a good service.

8.2 Ideally, a comparison website would cover the whole of the financial services market in a transparent and independent manner that would allow consumers to make a truly informed choice on which product best suits their needs. Generic advisers could then refer their clients to this website.

8.3 The FSA recognises the value of comparison information and provides its own comparison website within the “Moneymadeclear” pages. The FSA website is independent and not influenced by any commercial factors. However, it is limited in its range. At present, the FSA tables cover only pension annuities, mortgages, savings accounts, stakeholder and personal pensions, unit trusts and OEICS, ISAs, investment bonds and savings endowments. This range of products may increase in the future.

8.4 Currently, the FSA website omits consumer financial products such as life insurances, house insurance, credit cards and personal loans. There are also a small number of firms (named on the website) that exclude their products from the FSA website.

8.5 On the other hand, the commercial websites do cover a fuller range of consumer financial products as well as other products, such as utilities and mobile telephones. A few websites also claim to be whole of market. However, there is some concern that these commercial tables work in ways that are detrimental to consumers.

8.6 Some recent reports⁵ have raised concerns about commercial comparison websites. The reports suggest that the websites may:

⁵ See, for example, the Resolution Foundation report, ‘Compare and Contrast: How the UK comparison website market is serving financial consumers’ - http://www.resolutionfoundation.org/pdfs/research_report_webcomparison.pdf

- be opaque in explaining how they generate revenue and how their commercial relationships affect the content of their sites;
- require personal contact details to be provided, which then leads to the consumer being contacted and possibly pressurised into a sale;
- provide inaccurate or out-of-date information;
- refuse to be included within comparison websites.

8.7 Given the potential importance and usefulness of independent and impartial comparative information to clients of a GFA service, this is an area for further consideration by the FSA and others.

9. Conclusions

9.1 Evaluation of the prototype services shows that the approach set down in the advice protocols largely succeeded in enabling and encouraging clients to take action regarding their finances. The boundary with regulated advice was not generally seen as a significant factor. Even where experienced advisers had initial concerns about the boundary, these concerns diminished as the advisers realised how much help they could provide using the protocols.

9.2 However, the prototype services did not specifically set out to test the boundary between GFA and regulated advice and the advice protocols stopped short of the regulatory boundary. In particular, the prototype protocols prevented the advisers from making explicit recommendations, which included making a recommendation for a type of product. Furthermore, the prototypes used a mix of experienced and inexperienced advisers over a short period of time.

9.3 The effectiveness of a future GFA service could be enhanced by using advisers with a sufficient degree of training, and extending GFA towards the regulatory boundary through allowing explicit recommendations for types of products. In particular, a future service should be able to recommend a range of simple products, such as cash ISAs and term life insurance, which are important and appropriate for consumers faced with specific life events. There is some indication that potential clients of the GFA service would welcome such an extension.

9.4 As Annex 4 to the Interim report makes clear, and as is further demonstrated in the adviser and stakeholder feedback from the prototype services, the main difficulty in extending GFA to come closer to the regulatory boundary is the complexity of that boundary. Providing guidance to a consistent depth is difficult and may confuse both advisers and consumers. There is a clear need for the regulatory authorities to provide detailed guidance on what GFA can do without overstepping the boundary. Because GFA covers a range of topics regulated by the FSA and the OFT, and involves non-regulated areas but where there are legal and other implications, such guidance would benefit from being provided on a cross-government and other agency basis.

9.5 It would also be helpful if the FSA and others could consider the future role of comparison websites in providing GFA and, in particular, the concerns about the independence and transparency of these websites.

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February 2008