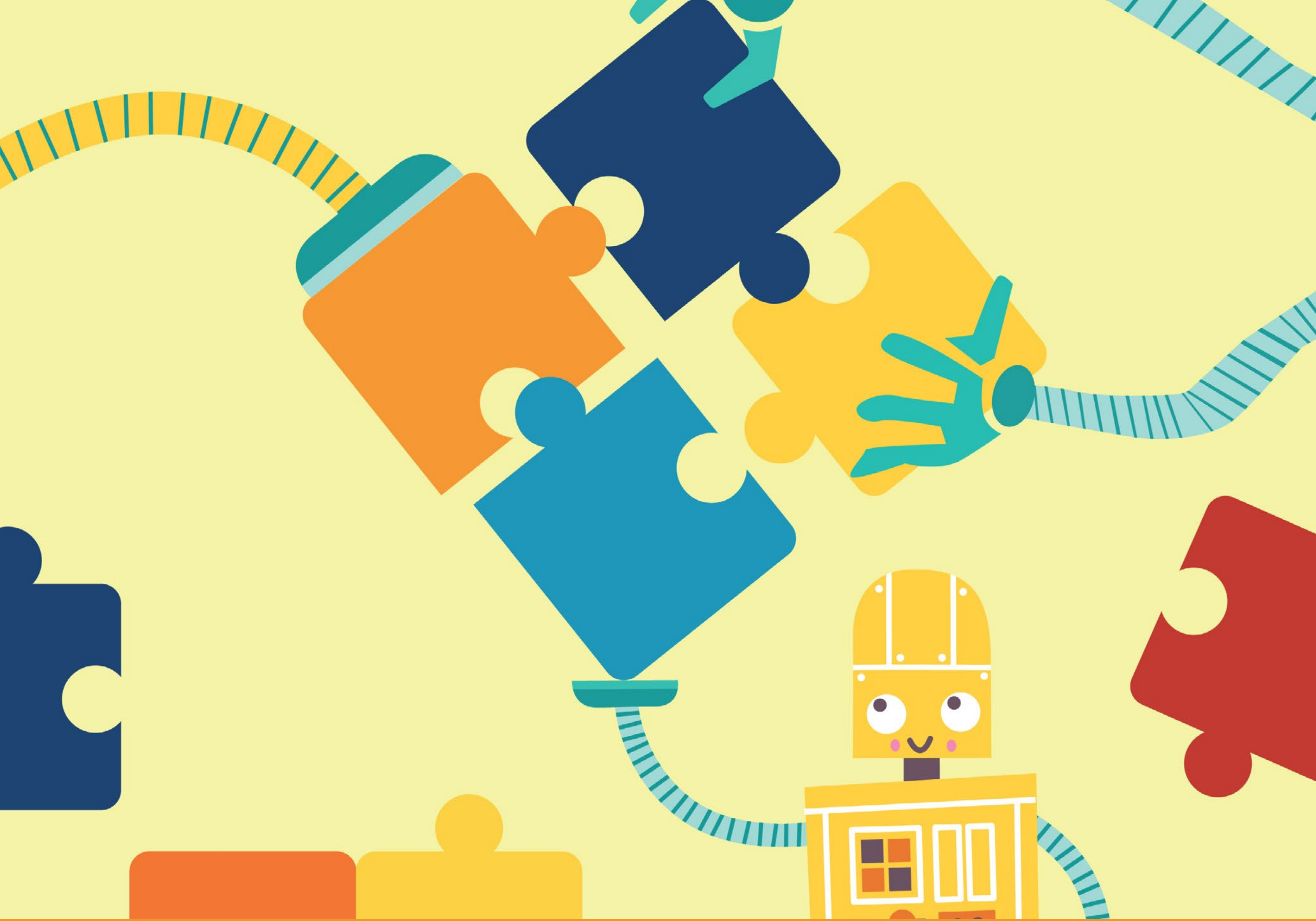
NEXTWEALTH

# Consumer Duty: Implications for the retail wealth management supply chain

November 2022

*A research report for financial advice professionals*



# NextWealth View

At NextWealth we want to help firms thrive amid disruption and one of the biggest sources of disruption is regulatory change. We are pleased to provide you with this report to provide industry and customer context to help you fulfill your obligations under the new Consumer Duty. The report is made possible through the generous support of:

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The report details findings of our research and provides useful guidance to firms as they consider how they will comply with the new Consumer Duty. Before sharing those findings, we wanted to share our view of some of the implications of this important regulatory change.

- Outsourcing and insourcing: At NextWealth we have tracked the rise of outsourced MPS on platform and expect a continued shift from adviser models and bespoke discretionary to discretionary MPS. Financial advisers will reduce the number of DFMs they work with as they look to develop fewer strategic partnerships to meet the needs of defined target markets. We will also see a rise in tailored models and insourced CIO as firms tighten their proposition and focus on delivering a cohesive and consistent customer journey.

- Tech enabled advice: There is a risk that Consumer Duty will reduce access to advice. Large firms are investing in hybrid or tech enabled solutions to address the widening advice gap. Simpler solutions for clients with simpler needs make sense. We have already seen a few tech enabled advice models emerge offering remote advice. This trend will accelerate.

- Audit trail: We will see more focus in financial advice firms to create audit trails for decisions and actions taken on behalf of clients. Most financial advice firms are already focussed on helping clients achieve desired outcomes, but documented evidence of this focus is lacking. This will put an onus on product providers to offer more transparency. Financial advisers will rely heavily on back office system reporting functionality.

- Adviser portals: Following on from the above, we expect to see a proliferation of tools and portals launched as firms race to meet the July 2023 deadline. For example, we'll see more adviser portals from DFMs to offer portfolio look-through and historic changes to holdings and rebalances. The same is true for providers of governed or insured products, such as smoothed funds.

- Platform nudges: Platforms will need to play a more active role in identifying poor outcomes and in preventing foreseeable harm. We think the platform should support financial advisers by using data analytics to nudge advisers to act when needed. Platforms can identify if there is a cheaper share class, if a charge looks out of line or if no change has been made to a client account for several years despite on-going charges being levied.

- Fee pressure and innovation in models: Focus on value means continued fee pressure across the supply chain. We'll also see innovation in fee models – such as greater use of tiered charging, cap and collar and even subscription fees. We also expect innovation in platform and provider charging – perhaps platform fees for clients and advice firms.

We think Consumer Duty and the focus on outcomes is an exciting change for our industry. Some advice firms are frustrated by the lack of clarity on how best to comply, but we are encouraged by the principles-based approach and the focus on client-centred culture.

We know from our research for this report the value advised customers place on peace of mind from good financial planning. The challenge now is to evidence that value.

**Heather Hopkins**

Founder and Managing Director
NextWealth

Feedback: enquiries@nextwealth.co.uk

# Introduction

This report details findings from research conducted by NextWealth on behalf of:

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It captures views from providers, advice firms and consumers.

The research was conducted on behalf of a group of asset management firms, DFMs and platforms and is kindly sponsored by abrdn.

The purpose of this research project is to help your firm:

- Collaborate with peers across the supply chain to ensure your firm's interpretation is in-line with others in the industry.
- Identify specific areas requiring focus for your firm's compliance, based on consumer and adviser research on the communications that are used to assess value.
- Contextualise your firm's response with an understanding of the expected implications of the new Consumer Duty for financial advisers, platforms, asset managers and DFMs.
- Allow firms to look forward to the implications of the new Consumer Duty on their businesses and across the retail wealth management supply chain.

The new Consumer Duty challenges all of us to collaborate to help customers achieve better outcomes. We are grateful for your support for this research and our event.

# Respondent profile and methodology

The results in this report are based on quantitative and qualitative research conducted by NextWealth and are informed by discussion of the findings at an industry event attended by asset management firms, platforms, DFMs and financial advice firms.

Quantitative Surveys

- Quantitative survey of 327 financial advice professionals (financial advisers, paraplanners and ops managers) in August 2022, with a top-up survey of 102 financial advisers conducted in October 2022
- Quantitative survey of 302 consumers paying for on-going financial advice, conducted September 2022

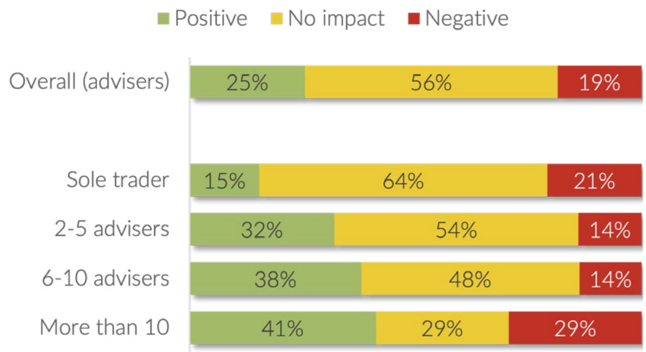
Qualitative research

- In-depth interviews with 10 financial advisers from the NextWealth Research Panel, representing a range of firms by geographic location and AUM.
- In-depth interviews with 10 advised customers and one focus group of 4 younger advised customers (aged 35-50). All interviewees receive financial advice on an on-going basis and have paid for advice in the past year. Advised customers had a minimum of £250k of investable assets outside of property

# 1. Industry Impact

- More than half of advisers expect Consumer Duty to have no impact on their business.
- Among those that expect an impact on their firm, more expect that to be positive than negative.
- Larger firms are more likely to anticipate an impact and almost a third say it will be negative.

**Figure 1:** Impact of Consumer Duty




*Source: Data from survey of 327 advisers conducted in August, 2022*

# 2. How prepared are advice firms for implementation

Our research confirms that the biggest gap in financial advice firms in preparing for Consumer Duty is gathering evidence to show firms are doing the right thing:

- Only one quarter of financial advisers are fully confident that they can calculate the expected total cost the customer will pay, despite this being required by MiFID II. A further 53% are confident.
- Only half of are fully confident or confident that they can track costs incurred in delivering service to clients. Yet, this may become a key ingredient to evidencing value – to the regulator if not to clients.
- Only 9% are fully confident they are able to benchmark fees and charges.

**Figure 2:** Adviser preparedness for Consumer Duty


*Source: Data from survey of 102 advisers conducted in October 2022*

We see a significant step change from the TCF rules in measurement to evidence that firms are doing the right things. Here, data becomes critical, at both a firm and industry level.

# 4. Addressing the four Consumer Duty outcomes

## 4.1 Products and services

In our research we found that consumers are broadly satisfied with the performance of investments recommended to them and the types of investment products recommended.

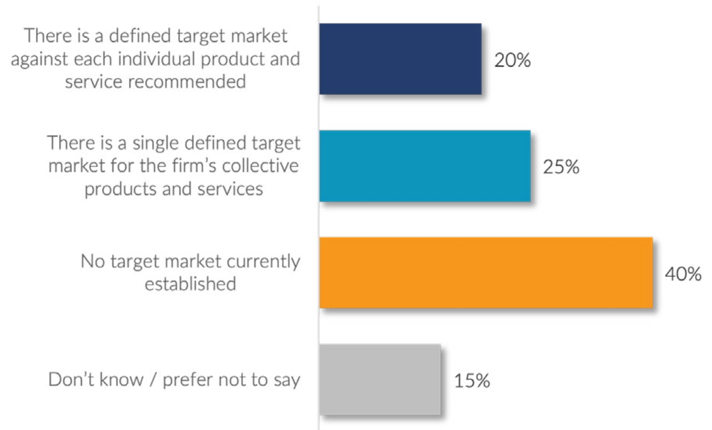
Consumers are most satisfied with performance when advisers set clear expectations.

> *"The value of having an IFA is having someone look after and make your money work for you. If it wasn't working, I would definitely not hesitate in questioning what was going on and looking for other advice, but I honestly don't know how I'd know if things weren't going in the right direction. I understand they're long-term investment so I'd trust him [my IFA] to put things right."*
>
> *-Consumer, 33 years, £250,000-£400,000 investable assets*

Key to meeting the product and service requirements of Consumer Duty will be for financial advice firms to clearly define a target market – or more likely markets – for the products and services offered. From our research, most advice firms are yet to undertake this exercise, at least on a formal, demonstrable basis.

- 40% of advice firms do not have a defined target market. Some told us that this feels at odds with their desire to offer a bespoke service. This desire to provide a bespoke service for every client is more common in small firms where consistency of approach is less challenging.

**Figure 5:** Advice firm target market by number of advisers




*Source: Data from survey of 102 advisers conducted in October 2022*

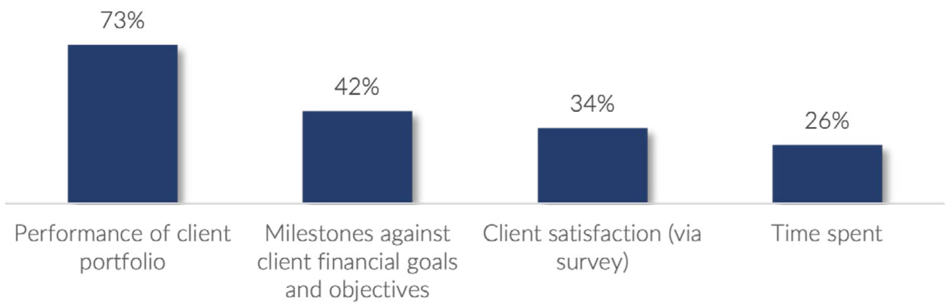
Consumer Duty will require advice firms to demonstrate that they have considered the needs of their target market and that they are delivering value to clients in that target market. With a defined target market, firms will have an agreed process, product range and pricing structure to follow, even if the specific outcome is bespoke to that client.

## 4.2 Price and value

The most common way that financial advisers demonstrate value is through investment performance. Both advisers and clients recognise that the real value of financial advice and financial planning are softer aspects such as a sense of financial empowerment and wellbeing.

We hope to see significant progress over the next year at measuring progress against goals to demonstrate value.

**Figure 6:** How are advice firms documenting value




*Source: Data from survey of 102 advisers conducted in October 2022*

While we all recognise that price is different from value, price is a core part is an important component and benchmarks for fees and charges are hard to come by. NextWealth has compiled data from 605 financial advice professionals to report average fees clients pay for on-going advice, funds, portfolio management and the platform.

The following two charts illustrate the spread of all-in on-going costs and on-going advice fees.

- 36% of advised customers pay between 140bps and 179bps all-in.
- 19% pay 200 bps or more and 13% pay less than 80bps.
- There are three distinct peaks in adviser on-going charges, at 50-59bps, 70-79bps and 100-109bps.
- The average fee for on-going advice is 68 bps but charges vary significantly by region.

**Figure 7:** Total fees, including advice, funds, portfolio management and platform

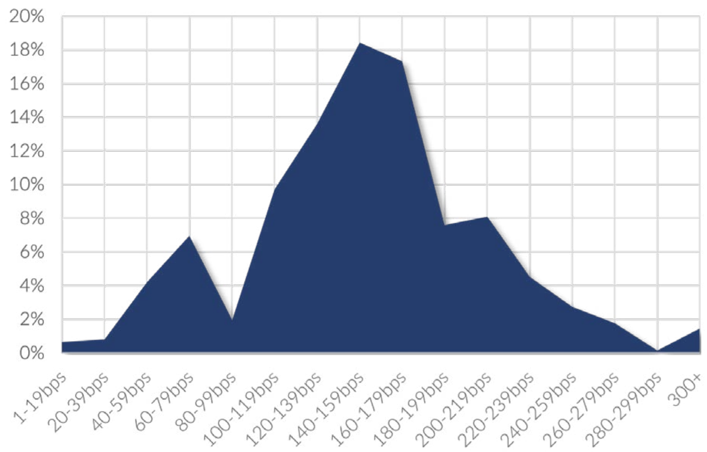
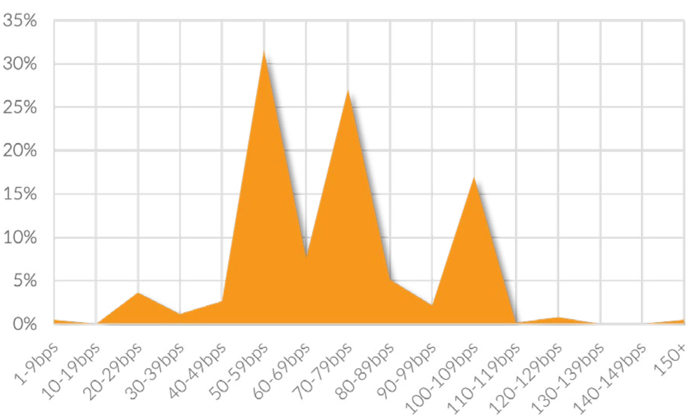



**Figure 8:** On-going advice charges




*Source: Data from survey of 327 advisers conducted in August, 2022*

## 4.3 Consumer service

In our interviews with financial advisers, a consistent theme emerged around the need for providers to respond more quickly to essential requests for information. Delays in this process can hold up the delivery of advice and can adversely impact client outcomes.

Advisers also feel providers can do more to uphold good client outcomes and avoid foreseeable harm to clients by improving the sharing of relevant information in a timely manner.

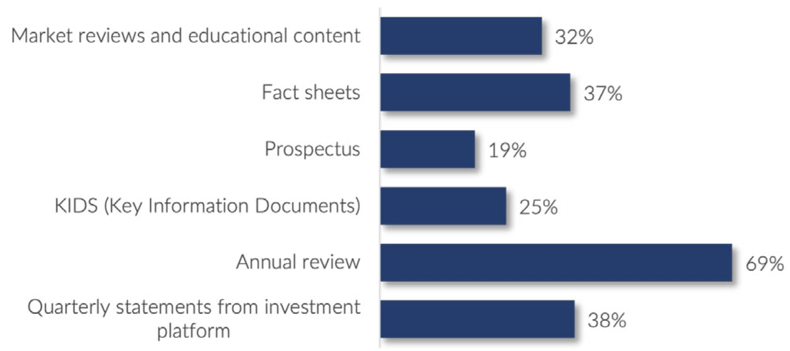
There is a need for collaboration across the supply chain to support better client outcomes. We hope to see platforms improve the utilisation of the vast amount of client data to which they have unique access and for the few providers with poor service levels to work with advisers to support positive client outcomes.

## 4.4 Communications read and understood by clients

A core part of Consumer Duty is to test whether communications are read and understood by customers. We think the focus should be on communications that consumers actually read. In our survey research and in-depth interviews, consumers said they are most likely to read the annual review document from the financial adviser and the quarterly statements from platforms.

As illustrated in Figure 13 below, outside of the annual review, advisers think less than half of the information provided to end clients is useful. Advisers see Consumer Duty as an opportunity to reduce the amount of disclosure and are keen to simplify the communications that are provided to enhance understanding.

**Figure 13:** Usefulness of information

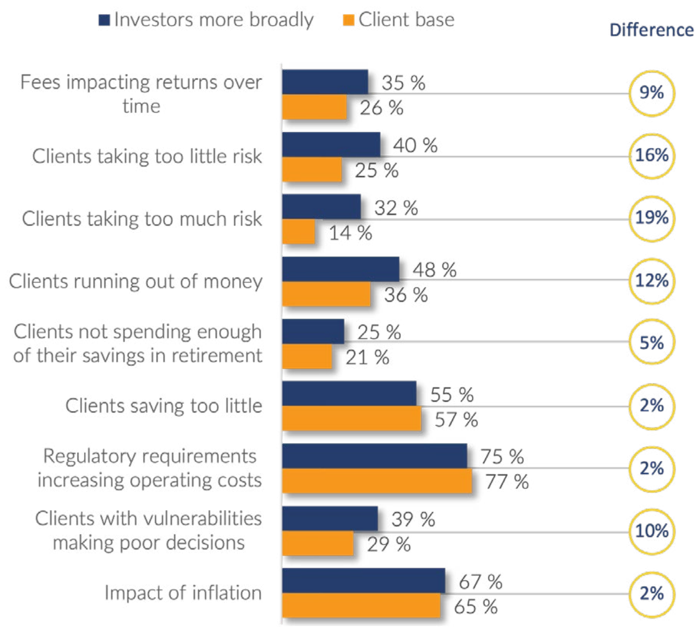



*Source: Data from survey of 102 advisers conducted in October 2022*

# 5. Avoiding foreseeable harm

We asked financial advisers about their concerns around foreseeable harm for their clients and investors more broadly. Financial advisers are most concerned about regulatory and inflationary costs causing harm to their own clients.

**Figure 14:** Financial adviser key concerns




*Source: Data from survey of 102 advisers conducted in October 2022*

# Conclusion

*"What gets measured gets managed."*

Attributed to business thinker Peter Drucker, this quote sums up the opportunity for Consumer Duty. The focus on outcomes and on-going measurement against delivering outcomes for clients, will force change.

While much work needs to be done between now and the July implementation deadline – we are optimistic that this work will herald a cultural change across our industry to collaborate to deliver better outcomes to clients.

Measurement requires data and that is a huge challenge for our industry. Platforms are the custodians of the assets but also of data. Platforms need to make better use of their data to nudge advisers to deliver better client outcomes and prevent foreseeable harm.

Financial advisers also need to think about what data they are capturing – and to focus more on soft data. Soft is hard – it's hard to measure soft facts but that doesn't mean it's not important. Our research reveals that until now, financial advisers have relied mainly on investment performance to evidence value. This must change. Investment performance is of course important. But the real value of financial planning and advice is peace of mind, a sense of financial wellbeing and as one of our consumer interviewees said, "being able to sleep at night."

Capturing soft data and measuring progress on soft outcomes is hard. That doesn't mean we shouldn't try. Effective use of tags in back office systems, tracking time, writing down and reviewing progress against goals – all of these things can help.

Consumer Duty is forcing all actors across the supply chain to measure progress against outcomes. We think the Consumer Duty will have a positive impact on our industry because "what gets measured, gets managed."

Thank you again to our partners on this research:

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We look forward to continuing to chart the retail wealth management industry's progress at helping clients achieve positive outcomes.

# The research does not stop there..

This report summary touches on the key findings from our Consumer Duty research.

The full research findings are available to purchase in an extended report.

If you would like to get your hands on a copy or have any queries regarding the extended research please get in touch at

enquiries@nextwealth.co.uk

Are you a financial advice professional? If so, you can stay up to date with all NextWealth insights through our Research Panel. To find out more head to

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