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Platform due diligence

Platform due diligence often gives rise to enthusiastic debate, which in our view is because there are so many advisers using platforms in so many different ways with a variety of clients, and there is no single formula which can be applied in all circumstances.

Guidance from product providers will, unsurprisingly, tend to recommend a focus on aspects of product design and delivery which favour their own unique selling points (USP's). However, independent advisers are required to deliver personal recommendations which are:

a) Based on a comprehensive and fair analysis of the relevant market; and

b) Unbiased and unrestricted.

Even though the Financial Conduct Authority's (FCA's) Thematic Review on Due Diligence (TR16/1) was rather concise it is still useful to review the comments and study their examples of good and poor practice, before working out what action may be necessary in your own firms.

But first, I think it is helpful to take a step back and consider exactly what 'due diligence' means. The FCA describes it as:

> "the process carried out by the firm to assess (a) the nature of the investment, (b) its risks and benefits and (c) the provider (to establish whether they believe it appropriate to entrust the provider with client assets)."

A web search for a deeper insight suggests that due diligence is:

> "an audit to confirm all facts, plus anything else deemed material" and "the care a reasonable person should take before entering into an agreement".

Therefore, advisers should be investigating the platform and the provider, understanding its risks and benefits, being clear about what the platform actually does, before those clients enter into an agreement to place their investments on that platform and pay charges for the services provided.

So, with that in mind, here are our Top 10 Tips for platform due diligence.

1. Focus on the client. As long ago as 2012 (FG 12/15) the FCA made it clear that platforms should meet the needs, objectives and requirements of your target clients. For the majority of firms, clients are likely to fall into more than one identifiable segment. It is therefore helpful to take a step back and describe your 'typical' clients, their personal and financial characteristics, their age and work status, their current and likely potential investment and product requirements, and the sums available for investing, now and in the future.

2. Be clear about your own firm's advice process and investment management style. Your platform research process should take account of whether you follow active or passive portfolio strategies, what range of tracker or multi-asset funds are available, whether you make use of outsourced solutions in the form of model portfolios or bespoke discretionary investment management services and how you make use of cash or natural income to deliver your clients' investment solutions.

3. Be prepared to research more than one platform solution. The analysis of your clients and your advice processes may lead you to consider researching one platform which is most likely to be suitable for younger clients who are building portfolios with smaller regular contributions, investing in low cost multi-asset funds invested in pensions and ISAs, and delivered through a light touch and low cost service proposition. A second platform would be more suitable for wealthy retirement clients drawing down tax efficient income and capital from pension, ISA and offshore investment bonds, using bespoke discretionary investment strategies to deliver the required outcome.

4. Cost. Price is not everything, and cheapest is not always best. On the other hand, the FCA dislikes clients paying for features and facilities from which they will not realistically benefit. So always ask whether higher levels of service and functionality will actually deliver concrete benefits to your clients, or whether your clients will be paying a premium for products, funds, facilities and services they do not need.

5. Platforms are just the start. Although a platform is 'just' an administrative tool, and a service rather than a retail investment product in regulatory terms, advice on the underlying retail investment products (i.e. pensions, investment bonds, funds, ETFs, investment trusts) must also meet requirements for suitability at the individual client level, and meet the tests for independence, where relevant.

6. Research criteria. Make sure you select relevant and client-centric features. For example, adviser charging options and online functionality are adviser centric features, whereas income payment options and access to relevant investment vehicles are client-centric. Additionally, ensure you understand the features on which you conduct your research and understand their assessment methodology, and what the different ratings, or no rating, actually mean and why this is important to your client.

[1] TR16/1 1.3.ii

7. Service. In TR16/1 the FCA noted that some advisers exhibited ‘status quo bias’ by failing to review their platform providers, if service levels remained satisfactory. Service is important to advisers and clients, but should it override all other possible selection criteria? If you use service ratings in your research, take time to understand the rating methodology, including how firms are included (or excluded), as in some cases an unrated company simply means that too few advisers responded to the survey, not that they actually have poor service levels.

8. Use a trustworthy data provider, who aims to cover a market as comprehensively as possible, to conduct your research. Some research systems, such as Defaqto’s Engage, cover the full universe of potential providers, while others only provide information on the largest or most popular adviser platforms. These tools will also address the FCA’s concerns over consistency in due diligence processes by providing workflows, research structure, repeatable process, as well as an audit trail to demonstrate your good practice.

9. Comprehensive and Fair. Third party research tools will often make a ‘product compare’ function available enabling advisers to set out a large number of relevant research features on a like-for-like basis, enabling clear and fair comparisons between providers and platform options.

10. Reviews. Defaqto research indicates that the most popular review frequency is annual, but whatever the frequency, commit to a regular formal review of the research, but also stay up to date with product and pricing developments so that you can quickly and easily identify platforms which remain suitable, or where alternatives may now need to be considered.

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[1] TR16/1 1.3.ii