

## Does your client and investment proposition need a PROD?

In January 2018, MiFID II introduced the 'Product Intervention and Product Governance Sourcebook' or PROD. This may sound like a handbook that applies to product providers and indeed it includes many rules for these firms; but it also includes sections that are relevant to advisory firms – or 'distributors' as the handbook inappropriately calls you.

The aim of the handbook is to ensure firms have good product governance. In advisory terms, this refers to the approach to providing advice to clients, including the design and implementation of the firm's centralised investment proposition (CIP), centralised retirement proposition (CRP), platform selection and initial and ongoing advisory services.

There are rules around understanding products and liaising with providers, but I want to focus on the advisory firm's proposition for clients. This is enshrined in PROD 3.3.15 R (1) which states that: "Distributors must have in place adequate product governance arrangements to ensure that ... the financial instruments and investment services they intend to distribute are compatible with the needs, characteristics and objectives of the identified target market".

### What does this mean in practice?

You must understand your client bank and target market, and design investment solutions – and advisory services – that work for these clients. This will inevitably involve platform selection as well. This means conducting a firm-level assessment of the client bank and the segments of clients that you have, rather than giving suitable advice to individual clients (which clearly you must still do).

### I am in a small firm, do I need to do this?

The handbook states that firms must comply with the PROD rules in a way that is proportionate and appropriate. Hence you still need to go through this process but it is likely to be less onerous than would be the case with a large firm.

### Don't we do this already?

You should have been doing this – it has been guidance for around ten years – but I would question how well firms are doing this. For example:

**Asset-based advisory services.** Many firms provide different levels of ongoing service dependent on the level of the client's investible assets. This is more of a firm-centric rather than a client-centric approach, as the level of assets is a poor indicator of the type of services that are appropriate.

**Platform selection.** Firms often select a single platform on the basis of a range of factors relating to the nature of the investment solution and ongoing services they want to deliver. This may be fine but it seems that sometimes this is more for the convenience of firms than the benefit of clients. I hear some advisers saying that platform costs are all fairly similar, which is simply not true. You should be looking for good value for money on behalf of your clients by seeking the most cost-effective platform(s) for the functionality, service levels etc you need.

### What do you recommend?

Firstly, segment your client bank. I recommend doing this at two levels – at an appropriate high level and also sub-segments. I think life stages works better than asset levels as a high level segmentation (see table).

Category	Summary	Possible investment solution	Platform selection	Advisory service
Young accumulators	Clients up to the age of 45/50 (typically) whose main focus is to build their wealth and save for retirement	Simple and low maintenance; eg multi-asset fund, MPS	Low-cost with functionality needed	Light touch with additional advice at major life events (eg marriage, job change)
Serious about retirement	Clients from 45/50 to five years before retirement who now need to be more serious about retirement planning	Probably still simple and low maintenance	As above	Moderate. Focus on cash-flow planning and advice about making up shortfalls

Glidepath into retirement	Clients between five years from starting to retire up until full retirement	Appropriate for decumulation; e.g. income-focus if going to natural income or different asset classes for 'pots' approach to decumulation	Cost-effective but has additional functionality for decumulation needed	Intensive. Cash-flow planning and advice about increasingly drawing income/capital and tax wrappers
Retirement income	Clients in full retirement	Dependant on income needs; may include annuity, drawdown as above etc	As above	Intensive if in drawdown to ensure sustainable income. Possibly IHT planning and care cost planning

Next, think about sub-segments. For example, you may have clients who run small businesses where remuneration structure and tax planning feature significantly. Or senior executives who have significant share-holdings in their employer and hence a bespoke discretionary management service might work well to manage out the imbalance over time.

I have given some examples but you need to see what works for your clients. If you undertake this segmentation process effectively, then the nature of the investment solutions, criteria for platform selection and the advisory services will probably be immediately apparent. This will help create an advice and service framework that is better geared for your client bank. Clearly you will then need to ensure individual clients receive suitable advice.

## How should I document this?

The FCA does not prescribe any approach to record-keeping but it does say you must keep a record of your process. I suggest you create your own matrix of clients as above although this will be much more detailed in practice once you have added in the sub-segments. I would then take the investment solution and platform selection columns information and create separate research and due diligence (R&DD) documents for each of these. The matrix comments could provide a context section at the beginning of your R&DD documents and it is these client segment needs that form the drivers for your investment solution and platforms selection R&DD. Similarly, for the advisory services column, I suggest you create a separate document with the rationale for the design of your service proposition for the client segments, using the matrix comments as a starting point.

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