Assignment 1 Coursework Guide

APRIL 2022 | SCQF LEVEL 9 PRACTICAL INVESTMENT PLANNING

Practical Financial Exams

Introduction

This document is in addition to the study text and Qualification Specification (QS), to provide further guidance to candidates in how to pass SCQF Level 9 Practical Investment Planning (PIP) Assignment 1 first time. This should be read in conjunction with your study text and the QS.

Syllabus as it Relates to Assignment 1

The Learning Outcomes and Performance Criteria in the syllabus that are tested by Assignment 1 are as follows:

2. **Synthesise professional, compliant, suitable investment plans for retail investment clients.**

   2.1 Produce a professional, compliant suitability report comprising a piece of innovative investment advice, the client's objectives, the reasons why the advice is suitable, and any disadvantages of the advice.
   2.2 Demonstrate the suitability of the advice via deterministic and/or stochastic cashflow models.

Learning Outcome 2 and its performance criteria therefore focus on what the Adviser needs to do once they have the client's agreement to proceed with the advice process, including researching the market, investment selection, tax-wrapper selection, suitability report writing, and cashflow modelling.

The FCA's 2017 Assessing Suitability Review, the FCA confirmed that of the 1,142 cases it reviewed, 6.8% of cases were either unclear or unsuitable. Both are breaches of COBS 9.2 as the firm has not taken reasonable steps to ensure the personal recommendation is suitable for the customer.

6.8% may sound small, but good SR writing is about more than providing advice that meets the bare minimum requirements set out in COBS. Just because a SR is compliant does not necessarily mean it is good practice, or that the Adviser is providing the client with a great service.

As per Learning Outcome 2, we expect advice to be more than just "compliant" and "suitable". We also expect it to be "professional".

While not a requirement to pass, advice should also demonstrate a degree of innovation; the ability to think outside the box. Where this is not evident in the report, candidates will need to show they can innovate in Assignments 2 and 3.

Understanding the Qualification Specification

The QS is a document which provides detailed guidance on everything you need to do to pass SCQF Level 9 Practical Investment Planning. Is the same document that our Assessors use to mark candidates' work. It is freely available to download via our website.

The key adjectives in the Learning Outcome and Performance Criteria used to describe what the advice and SR must be for Assignment 1 are "professional", "compliant", "suitable", and "innovative". These terms are defined in the QS as follows:

Professional	• The report is well-structured and easy to understand and navigate
Compliant	• The content of the suitability report is sufficiently compliant with COBS 9.4 • The recommendations are sufficiently justified according to the regulation in COBS 9.2 and guidance in COBS 9.3 • The report is in keeping with the Conduct Rules as detailed in COCON 4.1, and the FCA Principles for Business in PRIN 2.1 • The report is accompanied by relevant regulatory support documents • The report is accompanied by a list of documents which would be included on the client file, were this a real case
Innovative	• It is evident that the Learner has approached the assignment creatively, with an inventive take on investment planning
Suitable	• The recommendations are appropriate for the client, and sufficiently justified • The report contains deterministic and/or stochastic cashflow models which evidence the suitability of the advice

These definitions are non-negotiable. These are the definitions you must use when synthesising your financial plan. The QS then goes even further by breaking down the definitions of these definitions, acting as a "checklist".

Assessment is binary. As it relates to Assignment 1, either you meet every one of the checklist criteria, or you fail. The only exception here is the requirement for the report to be innovative, which as we've already stated, is broadly optional.

The checklist criteria are very comprehensive; well-prepared candidates should be able to easily check off the different aspects of their report against the QS and then pass first time.

Simply put: if you do not read the QS, and prepare your report in line with our expectations, you won't pass.

For some candidates, there is an overreliance on “what we’ve always done”. Rather than study to improve their compliance knowledge and SR writing skills to the point they are pass-standard, some candidates provide us with the same old reports they’ve always used which pass internal/external file checks because they meet the COBS requirements but lack the additional requirements for PIP as outlined in the QS. However, this doesn’t mean that existing templates and processes can’t be used as a starting point – often only very minor additions or tweaks are needed for pass-standard.

The Use of SR Templates

It is perfectly acceptable for candidates to use a SR template. It is good practice for firms to have a consistent format and branding of their reports and processes from one client to the next. Furthermore, templates can also ensure that all the key features, benefits, risks, and compliance points are covered in every report.

The two main reasons template SRs fail are:

1) A lack of understanding of how to use the template.
2) An overreliance on the template.

Your report still needs to comply with the requirements of the QS. For example, we require a summary page at the beginning. If your template doesn't have one, you will need to add one.

Furthermore, your report needs to be sufficiently personalised to the specific client, with reasons why which explicitly link back to the SMART objectives in the fact-find. Many templates contain generic reasons why **which are intended to be personalised**, and candidates have handed SRs in without personalising them.

This personalisation is broadly missing in two areas:

1) The reasons why are too generic, with no links back to the client's objectives.
2) Irrelevant reasons why, disadvantages, and risks are often left in.

A professional Financial Adviser or Paraplanner should be a surgeon when it comes to SR writing. They should be able to dissect it down to the individual words and sentence structure used and build it back up again from scratch. Another good analogy here is that of a computer engineer who builds computers and doesn't need to purchase a factory made one from PC World. But this is a real skill which takes time and dedicated study to master.

Template SRs can be a crutch that many Advisers have come to rely on because they're unsure how to construct tailored, personalised reports from scratch, and their continued reliance *prevents* Advisers and Paraplanners from developing advanced levels of proficiency.

Many templates also suffer from being written with a specific product or outcome in mind, which isn't conducive to SMART objectives-based financial planning which, by definition, is specific to the individual client. This is particularly the case where candidates are recommending more than one tax wrapper or investment strategy.

Furthermore, the use of templates can mean the Adviser is less familiar with the content of the SR, which can negatively impact on their ability to effectively present the advice at the presentation meeting, whereas they will know inside-out every inch of a report lovingly crafted from scratch.

As such, if you are using a template, make sure you know it inside-out, back-to-front, and upside-down. Make sure it meets the requirements laid out in the QS. And make sure it is sufficiently personalised.

Analysing Your Fact-Find

First and foremost, this is an investment planning qualification. We've developed our fact-finds to have an investment planning focus, the same way the CII develops the case studies in its AF exams to have a particular focus depending on the syllabus of the unit.

Our fact-finds will usually involve clients where pension planning is not an objective. This may be because they're a long way off retirement, they already have adequate plans or resources in place, or they are already comfortably retired. Where pension planning might cross over into a PIP fact-find would be where, for example, the retirement planning strategy has already been decided and you are purely providing investment advice.

The textbook doesn't cover estate planning or IHT in any depth, and in our fact-finds, we generally try to make clear that this is not an issue for the client. Clients will almost always have up-to-date Wills and Powers of Attorney in place, and no IHT issues to speak of. You therefore shouldn't need to worry about trusts or Business Relief. The exception here would be if, for example, a trust was already set up and you were purely providing investment advice.

Our fact-finds will usually involve clients who either have sufficient financial protection in place already, perhaps with a specialist Mortgage and Protection Adviser, and who do not wish to review this with you, or clients who have no need for protection planning. Therefore, you shouldn't need to worry about protection.

Where the client has a mortgage or other liabilities, you MUST consider the repayment of debt vs. investing. This is a regulatory requirement. However, you won't need to review the continued suitability of a client's existing mortgage, for example.

Specialist areas such as long-term care, equity release, and defined benefit pension transfers will not form any part of any of our fact-finds.

In the fact-find, there are three key areas that candidates may be unsure of, perhaps because they go deeper than most real-world fact-finds we see. These are income and expenditure, risk profiling, and investment preference.

Income and Expenditure

We've included full details of income and expenditure for each of our fact-finds, including an analysis. This is purely to evidence that the client has sufficient income to cover their expenditure now and in future. Any exception to this would be clearly outlined in the client's SMART objective, for example, the generation of a current income to plug an income/expenditure deficit.

Risk Profiling

You'll notice the risk profiling part of the fact-find is highly detailed, with a comprehensive risk profile established. You don't have to do any more analysis here – it's all been done for you. However, you may if you wish transpose the risk profile in the fact-find to an equivalent one used by your firm (e.g., what's "moderate" for us might be "risk profile 4" for you).

It's this part of the fact-find that intimidates some candidates, but there's no reason to be worried. All the complicated mathematics and cashflow modelling is doing is justifying the risk profile, and it's the risk profile you need to concern yourself with – not how we got there.

Investment Preferences

In each of our fact-finds, the client will provide their personal investment preference either for an advised portfolio, a managed portfolio, or a DFM. However, this is purely a personal preference and should not be interpreted as part of the client's objectives. As the Adviser, it is entirely up to you what you recommend.

You must consider your client's personal preference though. When writing the reasons why and disadvantages in your SR, if you have recommended a strategy which is compatible with the client's preferred investment strategy, this should be considered a reason why.

If you have recommended a strategy which does not reflect the client's preferred investment strategy, this should be considered a disadvantage, and you should have a good reason as to why you have recommended something against their personal preference.

Ethical and religious preferences, where present, must be considered.

Planning Your Report

When laying out your report, you should consider the layout detailed in the study text:

Section	FCA Requirement	PIP Requirement	Notes
Cover Page	No	No	Probably a good idea to have a cover page from a presentation perspective, although we're not going to mark you down if you don't.
Summary Page	No (yes for DB transfers)	Yes	This should include a summary of the advice, charges, and a general statement about risk.
Your Personal Circumstances	No	No	Completely optional, there are convincing arguments both for and against outlined in the textbook.
Your Objectives	Yes	Yes	Requirement confirmed in COBS 9.4.7. This can be copied and pasted from your fact-find, either in or outside the SMART table. You don't need to reword them – they're already in the client's own words!
Your Risk Profile	Yes	Yes	The investment recommendation needs to be compatible with the client's risk profile, so this needs to be in here somewhere. A summary of the risk profiling details in the fact-find, signposting to the full analysis, is fine.
My Recommendations, the Reasons for Them, and Their Disadvantages	Yes	Yes	Requirement confirmed in COBS 9.4.7.
Cashflow Modelling	No	Yes	This is Performance Criterion 2.2. We need to see a cashflow model evidencing the suitability of your investment advice. It must be stress-tested, and fully explained.
Additional Information	No	No	Basis of advice, remuneration method, and anything else from a typical SR checklist can go here.

This format is not a prerequisite, providing you have all the PIP requirements somewhere. We've seen some excellent reports which don't follow this exact format.

Cashflow Models

The Qualification Specification confirms that the report must *"contain deterministic and/or stochastic cashflow models which evidence the suitability of the advice… which demonstrate at least in theory that the investment plan has the potential to meet the client's needs and objectives."*

Our textbook includes an entire chapter on cashflow modelling, including a fully illustrated guide on how to build simple deterministic cashflow models ideal for demonstrating the potential achievability of investment objectives for retail clients.

The rules on cashflow models are as follows:

- There should be a basic explanation of what cashflow models are, their purpose, and the type(s) of models used. E.g., *"Cashflow models are graphical projections of what might happen in future with your investment portfolio. They help assess the realistic potential achievability of your financial objectives. The type of models we've used in your report are known as deterministic cashflow models, which means they are based on a set of fixed assumptions for inflation and future investment returns. They're by no means perfect but can be useful in helping to determine whether the recommended plan can meet your objectives in theory."*
- Any assumptions (for investment returns, inflation, etc.) must be justified, not simply asserted. E.g., *"I have assumed a future rate of CPI inflation at 2%, which matches the intermediate rate of inflation expected by the Financial Conduct Authority as published in its handbook"*)
- The models should be accompanied by a comprehensive explanation of what they show. E.g., *"The green line represents your portfolio starting at £97,000 (calculated as your £100,000 less your £3,000 initial advice fee). The orange line represents inflation starting at £100,000. As you can see, your portfolio is projected to rise in value more quickly than inflation, and at the end of your 10-year term, you are expected to have achieved real capital growth. It's worth remembering though that, year-to-year, markets will fluctuate. Some years your portfolio will rise and others it will fall, but we broadly expect it to average out at the annualized compound growth rate we have assumed."*
- Any deterministic models must be stress-tested, which means that an unfavourable scenario must be modelled and shown alongside the 'standard' models. This may demonstrate a 'fail' scenario communicating that there is no guarantee the client's objective will be met by the plan, should the assumptions in the original model not play out. Further, a caveat that the stress test is not necessarily a "worst case scenario" may help to further protect the Adviser.

Using Cashflow Modelling Software

Some candidates use cashflow modelling software which produces a 30 or 40-page auto-generated report, and this is provided as an accompaniment to the SR. While this can be a good place to start, on its own, this is highly unlikely to meet our requirements.

Here are some of the main reasons we have marked down assignments which have over-relied on one of these reports:

- The report is provided purely as an appendix and is not explained or referred to in the SR.
- The report provided focuses on lifetime cashflow planning, and completely ignores the client's stated needs and objectives.
- The report provided doesn't include any stress-testing for deterministic models.
- The report provided is too long and complex for a typical retail client to understand.
- Assumptions used in deterministic models for inflation, tax, and charges have not been explained. **As the Adviser, YOU are responsible for the advice, and if you're using assumptions within a deterministic model, YOU need to be prepared to defend their use!**

Relevant models should be copied and pasted from your auto-generated output into the SR with a clear explanation, as demonstrated above. Therefore, feel free to use one of these software-generated models. But make sure that you do so in a way which meets our requirements.

Given the support we provide to candidates to help them quickly and easily produce their own deterministic models using MS Excel, including comprehensive videos freely accessible on YouTube and an entire chapter in the textbook, alongside our clear expectations in the QS, we're unsure why we get candidates sending us these big reports at all, with nothing in the SR and none of our requirements met.

We're unsure if this is because candidates aren't reading the QS or the example SR in the textbook, but often there is a clear lack of awareness of our expectations when it comes to cashflow modelling.

Examples of Innovation

We often get asked for examples of innovation. We're pleased to provide the following examples:

- For a capital preservation objective, one candidate didn't invest all the money. She only recommended investing 80% of it as, according to her cashflow models, this was all that was needed to be invested to comfortably achieve the client's objective.
- One candidate recommended a passive advised portfolio featuring two funds tracking two difference indices for each asset class to further diversify risk.
- One candidate recommended a combination of smoothed funds in an investment bond to better meet the client's risk profile and diversify risk.

There are loads more where these came from. You don't need to reinvent the wheel, but at this advanced level of qualification, we expect candidates to be able to give us something more than a single fund in an ISA/GIA.

Other ideas for you (of the top of our collective heads) include:

- A managed portfolio featuring growth funds, value funds, and/or passive funds to provide diversification of investment strategy.
- An advised portfolio of single sector funds comprising a passive and active fund for each asset class.
- The use of investment bonds or structured products alongside ISAs and GIAs for tax wrapper diversification.
- The use of pension contributions to generate tax-efficient returns **where this could help the client meet their objectives**. This might be the case for a client who has reached state pension age and who is within their lifetime allowance.
- A combination of DFM and collectives. For example, for a larger portfolio, 50% DFM and 50% passive collectives to diversify investment strategy and reduce portfolio cost.

Investment Bonds Faux Pas

At PFE, we love investment bonds. They can help with the innovation criteria in some cases, for example, by allowing access to investments not available in other tax wrappers, or due to a specific tax planning strategy. But please note the following ways that could see you marked down:

1) Recommending additional lives assured when:
    a. There's no need for the additional tax-planning flexibility this offers
    b. There's clearly no insurable interest

    HINT: Capital Redemption bonds mature after a fixed term (say 105 years) and do not become automatically encashed when anyone dies, because there are no lives assured. This can help provide tax planning flexibility. However, this is not a life assurance contract, so it is not classified as long-term insurance for the purposes of, for example, the Financial Services Compensation Scheme.

2) Recommending an investment bond because it may not be considered when evaluating the client's assets to pay for care costs. This would be deliberate deprivation of assets and would result in an instant fail.

3) Attempting to justify the recommendation of an investment bond for a reason that isn't anything to do with the client's objectives. For example, waxing lyrical about how tax-deferred withdrawals can be made each year when the client has no requirement for this. We wouldn't fail a candidate for this but our spidey senses would tingle.

Linking Reasons Why to Objectives

Generic, unpersonalised reasons why are infuriating for us. It's so disappointing to see an otherwise great assignment let down in this area. Here, we have a table of some of the reasons why we've seen in actual assignments, why they're no good, and how they can be personalised.

Reason Why	Why It Was No Good	How It Could Be Personalised
[With a smoothed fund] *Funds are accessible with an expected growth rate.*	The concept of an expected growth rate wasn't explained, and neither was how it might help the client meet their capital preservation objective.	*The fund benefits from a smoothing mechanism which reduces the day-to-day volatility of your investment. This may help you meet your capital preservation objective with less risk and suits your limited investment experience. Please see below for more information on how this works.*
You did not want to be penalised by high encashment charges in the early years.	No client has ever said this. This is "putting words in the client's mouth". Where referencing something the client has said, the client's own words should be used.	*There are no fees or charges levied by the product providers should you wish to encash your investment earlier than planned, providing a greater degree of flexibility should your circumstances change in future.*
[An ISA] *is a highly tax-efficient way to invest.*	The candidate has failed to explain the benefits of tax-efficient investment to the client.	*An ISA is a highly tax-efficient way to invest. This potentially enables you to retain more of your investment returns (with less being paid out in tax) which can be used to help you achieve your capital preservation objective more efficiently.*
[The recommended platform provides] *a range of investment choices including 4,200 collective funds, investment trusts, Exchange Traded Funds enabling clients to meet their objectives.*	This is a product feature, not a reason to recommend the product.	*The platform can facilitate the recommended investment strategy and provides access to a wide range of other investment options. This may allow us flexibility to switch investments in future quickly and simply, to continue to meet your evolving needs, objectives, and risk profile.*
The portfolio is cost effective.	The candidate has failed to explain the benefits of a cost-effective portfolio.	*The portfolio is cost effective, which means that you'll be paying out less in charges than for a comparatively more expensive portfolio, allowing you to keep more of*

		your money to go towards meeting your capital preservation objective, which may increase your potential to achieve it.