OPEN DOOR POLICY

BUILDING PROPOSITIONS

Open Door Blog #3: Interconnectivity.

Clear, fair and not misleading

The phrase 'clear, fair and not misleading' often crops up in Regulator publications, it acts as a great litmus test for the advice process, especially when designing a charging structure. It makes a frequent appearance in the rulebook and is one of the 12 Principles.

Principle 7: A firm must pay due regard to the information needs of its clients and communicate information to them in a way which is clear, fair and not misleading. (PRIN 2.1.1)

Let's concentrate of clarity and fairness as I'm sure firms do not wish to mislead. The Consumer Duty's Price & Value Outcome as well as TR14/21 are good resources to make sure charges and advice solutions are clear. This is the area of advice where the regulator gave guidance to ensure that clients understood charging structures, which neatly leads into PROD which neatly leads into constructing a Centralised Investment and Retirement Proposition, leading on to investment and product solutions as well as software.

Everything is interconnected in an interconnectedness sort of way, so let's start with one, how do you ensure that your charges are clear and fair?

Open Door policy has experience in hundreds of consultancy sessions, looking at how a firms charge, the starting point is always two questions:

- What are your charges? (this is the easy one)
- How did you arrive at those charges? (not so easy)

The second question is frequently answered by "We've always charged this way" or "It's seems about right as most other firms do the same", so here are two more, which are similar but different:

- How do you know your charges are clear?
- How do you demonstrate that your charges are fair?

Key foundations

Now is the time to work through the key foundations:

- Identifying the cost of manufacture
- Setting minimums
- Setting thresholds

The cost of manufacture involves taking a theoretical charge per hour (have a look at the FCA's Data Bulletin Number 7) and multiplying it by the amount of time it takes to conduct an initial and ongoing advice process. But in doing so, consider the time it takes to conduct the advice process remembering Hofstadter's Law.

Hofstadter's Law: It always takes longer than you expect, even when you take into account Hofstadter's Law.

And it does, firms tend to underestimate the time it takes to deliver their advice which makes the task of getting it documented and then finding inefficiencies to streamline the process so important. It's very common for decision makers to be surprised at the results of this exercise, especially after realising their minimum charges are a lot less than they should be.

Once the cost of manufacture is identified it will highlight what your minimum charge should be, and if you know your minimum charge, you know the threshold amount of investment. For example, a threshold amount £95,000 will generate a minimum charge of £1,900 if the initial charge is 2.00%

Minimum £ charge (cost of manufacture) / initial % x 100 = threshold investment amount
£1,900 / 2.00% x 100 = £95,000

If you know the threshold amount of investment you can compare that against your client bank to see if it's representative and proportionate. This goes some way in demonstrating that your charges are clear, fair and not misleading. Everything is interconnected in an interconnectedness sort of way.

Decumulation

Should your charges for post-retirement client be different? Income in retirement is an area that the regulator has concentrated on:

- Focusing on advice received, retirement income and retirement risk
- Stressing the need for good advice at the point of accessing income
- Making sure firms have sufficient systems and controls in place

It might be time to look at your decumulation advice process now and how you charge for this.

If you undertake a cost of manufacture exercise for clients in the accumulation market then given the change of risk, administration and monitoring for a decumulation client should you also consider a similar exercise?

So we're naturally leading into the decumulation strategy and what that looks like, how you accomplish a sustainable income, risk management and software usage.

But how much you charge is dependent on time x hourly rate so what strategy do you employ, how do you build your Centralised Retirement Proposition, how long does it take, can it go better/faster with software. What about aggregate charging and looking at the complete advice chain, what is the most appropriate investment solution and product solution, how much do they cost and what is therefore the overall big picture? It's all connected and should not be taken in isolation.

These things and much more can be addressed, organised and documented by well thought out Propositions

- Price and Value (charges) Proposition
- Centralised Investment and Retirement Proposition
- Consumer Duty Proposition

If challenged you have an overarching strategy which not only addresses individual issues, but shows the effect they have on each other.

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