FSA factsheet for

Financial Advisers

Financial Services Authority

Improving the quality of your advice process – Recommendations (including research)

This factsheet is for you if:

- **you provide financial advice to retail clients (known as 'private customers' under the old Conduct of Business rules).**

This is the fourth of a series of factsheets that we are publishing over the coming months. The factsheets focus on the different areas of the advice process, that we reviewed in the firms visited and mystery shopped during the Investment Quality of Advice Processes II project. We published the detailed findings of the project on our small firms website on 6 August 2008. In addition to this factsheet, we have published three others, one focusing on quality of advisers, the second focusing on impartiality of advisers and the third focusing on assessment of customer needs. All three of these factsheets highlight examples of good and poor practice.

The examples outlined below are designed to help firms consider their own processes for conducting research and making recommendations to clients. There may be other ways of achieving the same outcomes and complying with our rules and principles and you should consider the relevance of these examples to your business, as you may choose an alternative approach.

In this factsheet:

- Recommendations
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- Examples of poor practice
- Next steps

Recommendations

When making a recommendation to a customer, do you:

- ensure that you have captured all the relevant "know your customer" information before you make any recommendation?
- recommend a product, fund or service to match the customer's attitude to risk?
- recommend the most appropriate product and provider and explain your decisions to your customer?
- consider affordability, debt repayment, the impact on benefits and tax implications as part of any recommendation?
- provide the level of service you committed to in your disclosure document and make appropriate outsourcing arrangements where your firm has limited resources in some areas?

Research

You must ensure you conduct adequate research and retain sufficient evidence of that research to support your recommendation. Are you confident that you:

- make an adequate comparison of product providers across the market to be able to select the most appropriate one?
- retain sufficient evidence of the research carried out to support your recommendation and explain to the customer why a particular provider, fund or portfolio of funds was selected?

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Examples of good practice

- Firm A had considered what its limitations were in terms of managing customers' portfolios, and had a policy where if a customer had a portfolio greater than £100k the advisers would have to discuss the case with the Director to consider an external fund manager to manage the portfolio. This was influenced by the fact that the firm believed that it could only review a portfolio on a quarterly basis and did not have the resources to do forward-looking research. The firm would also consider if discretionary portfolio management was the most appropriate route for its customers.

- Firm B used diagrams to help explain to its customers its financial planning strategy, prioritise the customers' needs, and explain the different risks associated with each recommended product and how these matched with the customers' attitude to risk. In its recommendations, the firm considered having emergency funds to be of the highest priority, and this was reflected as being the foundation in its illustrations.

- When discussing the merits of repaying debt, the adviser at firm C asked the customer for the interest rates being paid on each debt and used these to justify whether it was better to save, invest part of the capital or repay the debts. The adviser provided a print out, detailing the rates of interest available from bank accounts and discussed notice periods and rates, and if they were branch or internet based. The adviser recommended the debts to be repaid and to save the surplus money in a Cash ISA.

- Firm D carried out regular research on all products, but additional research and more regular reviews would be carried out for the higher risk or more specialist funds/products to identify new investment opportunities and/or to make appropriate changes to the customers' existing portfolios. This service would be agreed at outset depending on the needs of the firm's customers.

- Firm E categorised its customers' portfolios across five risk categories, based on the particular funds invested in, so that the firm could monitor their performance more easily and advise its customers accordingly. Customers would get one free review a year but could opt to pay to receive more regular reviews, which consist of the firm reviewing the portfolios in light of a number of factors, including changing market conditions. The firm would contact the relevant fund managers to explore any under-performance before making decisions whether to recommend that funds are switched.

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Examples of poor practice

- Discussion with an adviser at Firm F revealed that he would only compare up to three product providers to determine which one was the most suitable; this raised the question whether the firm, which held itself out as being independent, was actually providing a whole of market service.

- At Firm G, there was an over-reliance on its customers confirming that their investments were affordable rather than the firm undertaking an analysis of income versus expenditure to assess affordability before making a recommendation.

- When recommending an investment bond and an ISA to a customer who had a lump sum to invest for growth, the adviser at Firm H failed to adequately establish the customer's attitude to risk and asked the customer to pick his own funds from a 'Top Funds Guide' without making an appropriate recommendation.

- The adviser at Firm I recommended an investment bond and underlying funds consisting of 70% being invested in equities and 30% in corporate bonds, despite having assessed the customer's attitude to risk as 'Cautious', and the customer clearly stating that he did not want any risk of capital loss. The adviser told the customer that an ISA was not suitable as the customer was a basic rate tax-payer. The adviser did not give any consideration to whether the customer should repay the residual balance on his mortgage.

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Next steps

Over the coming months we will be publishing further examples of good and poor practice on the following subjects; communication, systems and controls including management information, and post sale. We would encourage you to familiarise yourself with these examples to ensure that your firm has good Quality of Advice Processes in place.

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