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Financial Advice Market Review – Call for Input

London, December 22nd 2015

Dear Sirs,

We welcome the publication of the *call for input paper* (the "***Consultation Paper***") *on the Financial Advice Market Review* (FAMR) by HM Treasury and the FCA (the "***Authorities***"). We appreciate the opportunity to provide you with our comments.

Introduction

Markit[1] is a leading global diversified provider of financial information services and financial technology solutions.[2] Founded in 2003, we employ over 4,000 people in 11 countries and our shares are listed on Nasdaq (ticker: MRKT). Markit has been actively and constructively engaged in the debate about regulatory reform in financial markets, including topics such as the implementation of the G20 commitments for OTC derivatives and the design of a regulatory regime for benchmarks. Over the past years, we have submitted more than 130 comment letters to regulatory authorities around the world and have participated in numerous roundtables.

In the context of the Consultation Paper, Markit's most relevant service is our Markit On Demand service which supports mostly investment managers, wealth managers, and brokers in creating solutions to facilitate their clients' investment decisions.[3] As a managed technology service working closely with our customers, we create innovative engaging designs that are easily implementable and support investment decisions. We believe Markit is one of the world's largest employers of web designers focused solely on the presentation of financial information and workflows, and we are expert in presenting complex information so that users can understand and use it to make informed investment decisions in a timely manner. During a typical week, our services support more than 2.3 billion page views of dynamic content and more than 2.5 million unique users log into the pages we host. Markit On Demand's unique position as the provider of technology services to a large number of asset managers and other investment professionals in numerous jurisdictions means we have broad-based experience of how financial institutions connect and interact with their clients.

[1] Please see www.markit.com for further details.
[2] We provide products and services that enhance transparency, reduce risk and improve operational efficiency of financial market activities. Our customers include banks, hedge funds, asset managers, central banks, regulators, auditors, fund administrators and insurance companies. By setting common standards and facilitating market participants' compliance with various regulatory requirements, many of Markit's services help level the playing field between small and large firms and herewith foster a competitive marketplace. For example, Markit's KYC Services provide a standardised end-to-end managed service that centralizes "Know Your Client" (KYC) data and process management.
[3] See https://www.markit.com/product/markit-on-demand for more details.

Comments

We agree with the Authorities that the way that people seek financial advice is changing. Technological, regulatory, and demographic change are driving new techniques that people use to interact with the financial industry and the way that they think about advice and how they access it.

Please find below Markit's responses to several of the questions asked by the Authorities in the Consultation Paper. Our views are based on the experience we have gathered working with our many clients in North America and Australia as well as the feedback we have gathered when working with potential users of our services in Europe. We would generally recommend that the Authorities aim to develop a framework that allows people access to a flourishing digital market and enables the benefits of technical solutions built for higher net worth individuals to be made available, with the appropriate protections, to people with fewer assets. We believe this would help reach a larger number of potential investors who may benefit from advice and guidance, but, with fewer assets, advisors may not target them specifically.

Such a framework should also cater for people throughout their lives, including periods of accumulation and of decumulation of wealth. We believe that investors need to be able to – and be encouraged to – stop seeing financial planning and advice as something that happens only as a one-off (i.e. a decision that is made and then forgotten about). Instead, advances in information technology now make it much easier to maintain a continual engagement and access to information about the performance of investments and initiate changes over time whenever desired or necessary.[4]

<u>Question 2</u>: Do you have any thoughts on how different forms of financial advice could be categorised and described?

We believe that the categories set out in the Annex of the Consultation Paper provide a helpful template for differing kinds of advice and are a useful reflection of the variety of advice that might be available.

However we recommend that the categorisation of the assistance available to investors specifically include "education" and "guidance", which is something many people browsing digital investment services are looking for, and which is the first step to developing more sophisticated investment behaviour. We also urge the Authorities to make it absolutely clear what kind of license is required for each category and ensure that a clear line is drawn between education, guidance and formal advice.

<u>Question 4</u>: Do you have any comments or evidence on the level of demand for advice from sources other than professional financial advisers?
<u>Question 5</u>: Do you have any comments or evidence on the types of financial needs for which consumers may seek advice?

The Authorities state that "some consumers make at least some of their financial decisions independently, using generic advice or using publicly-available information".[5]

From our experience we have observed that, even if they are seeking advice, users of the websites we have designed and host often also want to:

1) Educate themselves on an issue;

[4] Although it is important investors are fully aware of any costs of making changes to investments.
[5] Consultation Paper page 9.

2) Research possible solutions; and
3) Monitor the effectiveness of a choice they have made over time.

We believe that it is important that financial websites provide access to all of these functions, regardless of whether individuals seek advice or not. A recent study supports this view and also found that, while technology and social media are ingrained into the lives of younger investors, all age groups can make use of, and benefit from, information technology.[6]

Furthermore, through our experience working with clients that provide products to the retail market, we have found digital contextual education, including continued contextual education through the process of investment decision making, to be more effective than generic education that is provided separately from an investment decision.

__Question 6__: Is the FCA Consumer Spotlight segmentation model useful for exploring consumers' advice needs?
__Question 7__: Do you have any observations on the segments and whether any should be the subject of particular focus in the Review?

We believe that the FCA consumer segmentation, as set out in the Consultation Paper, broadly captures the groups of people who may be seeking, or could benefit from, financial advice and guidance. However, we are concerned that it does not recognise some of the complexities of real life where people who could appear to be of similar background may actually be facing very different investment needs. This is because the FCA segmentation model does not seem to fully consider the objectives of savers and the circumstances of the individual (for example, the number of children or the number of earners in the household). These characteristics can vary between people who appear to be in the same category and could affect significantly which investments are most suitable for them. For example, some might have inherited money while others might have children heading to university in the near future. We believe that recent changes in the UK, including auto-enrolment or the provision of more flexibility around drawing down pensions, are likely to further to impact this.

We also recommend that any segmentation consider the fact that people of different ages and backgrounds are likely to be more comfortable with different types of portals. For example, younger, more affluent people are more likely to engage through mobile devices or social media, whereas others may prefer other kinds of contact.

__Question 8__: Do you have any comments or evidence on the impact that consumer wealth and income has on demand for advice?

We believe that there is a minimum amount of savings or investments below which advice must be seen as prohibitively expensive. This has been evidenced in some recent research that found that only 6 percent of British people felt it was worth paying for advice on £30,000 of savings and were only willing to pay an amount of £314 for advice on a pot of £250,000.[7]

It is our experience that, generally speaking, individuals from households that fall into the higher income categories tend be more time constrained and so the lack of facilities that allow them to access advice and

[6] https://www.accenture.com/t20150626T121140__w__/us-en/_acnmedia/Accenture/Conversion-Assets/DotCom/Documents/Global/PDF/Dualpub_8/Accenture-Generation-D-Europe-Investor-Survey.pdf
[7] https://www.aegon.co.uk/news/media-centre/pressreleases/cost-of-advice-is-major-sticking-point-for-consumers.html; Also see http://www.money.co.uk/press/half-of-those-making-pension-freedom-withdrawals-will-not-pay-for-advice.htm

check on investments quickly could be holding them back from seeking advice. We believe that the broader availability of high quality robo-advice and web portals could help address this issue.

***Question 9*: Do you have any comments or evidence on why consumers do not seek advice?**

We broadly agree with the reasons set out in the Consultation Paper for why consumers might not seek advice. In addition, we believe it is also important to consider that some forms of advice or guidance can involve a lengthy process and be difficult to follow up on a regular basis. In this context we would like to highlight that technology can provide an efficient process that is much easier to follow up and remain engaged in (for example, automatic notifications could be sent to update when an investment plan is on or off track).

***Question 10*: Do you have any information about the supply of financial advice that we should take into account in our review?**
***Question 11*: Do you have any comments or evidence about the recent shift away from sales based on professional advice, and the reasons for this shift?**

Since October 2012 the auto enrolment scheme has increased the number of people receiving a workplace pension and this may be effect whether people believe they need to seek advice or not.[8] Also the banning of the commission-based sales model at the end of 2012 demonstrated to investors the costs associated with advice which, given the long dated nature of the value of the advice, could have created further reticence around engaging professional advice.

However, according to one study,[9] of those people who had money to invest but did not seek advice, the vast majority either did not think about advice or preferred other sources of information.

We would therefore recommend that the Authorities consider the educational benefits that web portals and robo-advice can provide for people, even when they are not seeking advice.

***Question 12*: Do you have any comments or evidence about the role of new and emerging technology in delivering advice?**
***Question 13*: Do you have any comments on how we look at the economics of supplying advice?**
***Question 14*: Do you have any comments on the different ways that firms do or could cover the cost of giving advice (through revenue generation or other means)? Do you have any evidence on the nature and levels of costs and revenues associated with different advice models?**
***Question 15*: Which consumer segments are economic to serve given the cost of supplying advice?**

We believe that there are numerous potential benefits from applying new technology to assist consumers in their investment decisions, many of which have been well debated. However, this debate often overlooks the potential for less affluent investors to benefit from systems that have primarily been developed for higher net worth individuals. This is because technology and platforms originally developed for higher net worth individuals can, for relatively low marginal costs, be extended to work for other markets. It is the potential scalability of such solutions that means services could become available for the greater number of individuals with less complex needs (or lower investment amounts) that would otherwise not attract developers because of high costs of developing specific solutions. We therefore believe that the regulatory framework should encourage (for example by making it simple to extend services to different target markets) this kind of cross subsidisation.

[8] For example: https://www.gov.uk/government/news/standing-ovation-as-auto-enrolment-hits-5-million-and-auto-transfer-launch-plans-are-unveiled
[9] http://www.cii.co.uk/media/5139793/pfs_rdr_consumer_report_feb2014.pdf

***Question 16**: Do you have any comments on the barriers faced by firms providing advice?*
***Question 17**: What do you understand to be an advice gap?*
***Question 18**: To what extent does a lack of demand for advice reflect an advice gap?*
***Question 21**: Which advice gaps are most important for the Review to address?*

A wide variety of portals open and available to potential investors are likely to provide a level of education that may not be available today. Simple to use, accessible websites can allow investors to receive examples of different investment options open to them and enable them to either make a more suitable investment decision or realise that it would be worth seeking more tailored advice.

We believe that the level of financial literacy in the broader population is generally low and that web portals, if appropriately designed, could help address this problem. However, the lack of regulatory clarity around the classification of these services can, in our experience, stop providers well short of being able to provide any meaningful insight, education or guidance. We therefore encourage the Authorities to provide the clarity that would allow portals to offer contextual information, education and customised guidance for potential investors prior to any sales process and formal advice process being offered.

***Question 22**: Do you agree we should focus our initial work on advice in relation to investing, saving into a pension and taking an income in retirement?*

Yes, we agree with this approach which appears to focus on the areas where people will need to take more personal responsibility for their retirement provision and where potential investor detriment exists.

***Question 23**: Do you agree we should focus our initial work on consumers with some money but without significant wealth? What exact income/wealth thresholds should we use to determine which consumers we will focus on?*

As set out above, research suggests that advisors are not willing to offer advice for investors with savings and investments below £30,000 while investors with less than £50,000 to invest would typically see the costs of advice as too high to be worthwhile.[10]

In line with our other comments, we would suggest that the Authorities consider how the educational benefits of web portals and robo-advice can be maximised and how systems developed for higher net worth investors could be easily adapted to meet the needs of investors with less investible funds for low marginal costs.

***Question 24**: Are there aspects of the current regulatory framework that could be simplified so that it is better understood and achieves its objectives in a more proportionate manner?*
***Question 25**: Are there aspects of EU legislation and its implementation in the UK that could potentially be revised to enable the UK advice market to work better?*

As we have stated above, we believe that the Authorities should provide greater clarity to the industry as to what is “guidance” or “education” and what will be seen as regulated advice. Clear markers between categories would help. We believe that while investor protection is absolutely vital and asset managers should take

[10] https://www.aegon.co.uk/news/media-centre/pressreleases/cost-of-advice-is-major-sticking-point-for-consumers.html; Also see http://www.money.co.uk/press/half-of-those-making-pension-freedom-withdrawals-will-not-pay-for-advice.htm

responsibility for the information they provide to their clients, an overly protective system, especially around educational material, leads to detriment.

<u>Question 29</u>: To what extent might the different types of safe harbour described above help address the advice gap through the increased incentive to supply advice?
<u>Question 30</u>: Which areas of the regulatory regime would benefit most from a safe harbour, and what liabilities should a safe harbour address?

We agree that safe harbours can provide excellent testing grounds for innovative approaches and we believe that our experience and expertise would be helpful. Therefore we would be happy to work with the Authorities in developing them. We would also encourage the Authorities to consider how the development of financial advice could benefit from the Regulatory Sandbox initiative announced by the FCA recently.[11]

<u>Question 36</u>: Do you have any comments on the extent to which firms are able to provide consistent automated advice at low cost? Are you aware of any examples of this, either in the UK or other jurisdictions?

In the UK, LV recently launched Clear Online Retirement Advice (Cora). Cora aims at lowering the personal advisor cost by providing a simple limited automated advice service, but still allows LV customers to get further support via a phone line to aid the process. This is an example where technology has been utilised to lower the cost if the needs are simple and limited which is the market segment least supported at the moment.

We would be happy to discuss our experience developing web portals in other jurisdictions.

<u>Question 37</u>: What steps could we take to address any barriers to digital innovation and aid the development of automated advice models?

In order to promote the ability of web portals to be able to provide information in the form of education or guidance, the Authorities should consider whether it is possible to develop a standardised form of such information. This might work in a way similar to KIIDs which are standardised for each financial product. For web portals, a standardised presentation of generic options for answers to predetermined questions could be developed that would provide more certainty as to what was being offered to the user was guidance and did not constitute a personal recommendation.

<u>Question 38</u>: What do you consider to be the main consumer considerations relating to automated advice?

We believe that it is vital for the FCA to provide as much clarity as possible around what is regulated advice (including what is simple advice and fuller programmatic advice) and what is guidance or education in order for the market to be able to provide innovative solutions. We recommend the Authorities also ensure that when solutions are provided for high net worth clients, they can be easily rolled out for less lucrative markets because of the lower marginal costs of doing so (compared to building new bespoke solutions). We further recommend that any regulation established by the Authorities focus only on the form of the advice and suitability to allow digital innovation to focus on solving the problems of how to get investors to access it. Finally, it is important that firms looking to move into the digital space are able to use third party expertise and shared

[11] https://www.fca.org.uk/your-fca/documents/regulatory-sandbox

solutions. This means that the solutions offered are likely to be of higher quality as firms can focus on the actual offer to the client rather than having to reinvent and duplicate services and recruit their own technical experts.

Demographically, a recent report indicates that 87% of high net worth individuals (HNWI) under the age of 40 in the US expect to conduct most or all of their wealth relationships digitally in the future.[12] The report also identified a higher proportion of this same age group as having less confidence and trust in their wealth management firms. Estimates from the report indicate that US HNWI individuals are willing to allocate up to $1.7 trillion to automated advisor models by 2017 (compared to $8.2 billion gathered in 2014). This combination of factors appears to indicate opportunities for digitally driven, automated advice solutions with sufficient flexibility for the more complicated scenarios of a HNWI. Conversely, those automated advice solutions will also need to provide sufficient transparency around their methodology, fees and other relevant information to provide these HNWI individuals with a sufficient level of confidence.

Some conclusions could be drawn from these findings for individuals with lower levels of investable assets. We believe confidence in wealth firms is at least as important as it would be for HNWI (who are likely to have a greater level of knowledge, or at least comfort, in dealing with their investments) so it is possible to recognise the role and value played by the firm. So while automated advice solutions may simplify the process around long term investment, sufficient education and disclosure remain necessary.[13]

<u>Question 41</u>: What steps should we take to ensure that the quality and standard of advice is appropriate as a result of any proposed changes?

We believe that a holistic approach that considers the full spectrum of education, guidance and personalised advice would be most useful. Included in this, particularly for advice, the categorisation needs to specifically consider the objectives of the investor and their own personal circumstances, such as the overall amount of assets to invest and the proportion of investable assets they are seeking to use.

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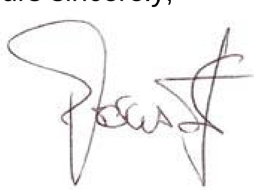
We hope that our above comments are helpful to the Authorities. We would be more than happy to elaborate or further discuss any of the points addressed above in more detail. If you have any questions, please do not hesitate to contact the undersigned or David Cook at david.cook@markit.com.

Yours sincerely,



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[12] United States Wealth Report 2015, Capgemini.
[13] Notably, the report also points out that 83% of HNWI under the age of 30 see availability of quality education as a top concern.