CHALLENGE AND OPPORTUNITY

THE IMPACT OF THE RDR ON THE UK'S MARKET FOR FINANCIAL ADVICE

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The unintended consequences of the RDR initiative, accompanied by rapid change in technology and social media, is likely to further extend the "advice gap", leaving aside those who have too few assets to merit attention from professional advisers, though they may well be in need of financial advice. This cannot be a desirable outcome. And surely was not the intended legacy of RDR? But the good news is that the massive shake-out in the industry will create opportunities for the more well qualified and sophisticated advisers who can genuinely add value with their client propositions – and they will be aided by the huge increase in transparency afforded by the end to platform rebates and trail commission. The fittest will survive, and that must be good for something as important as long-term wealth accumulation.

i. Advisor numbers fell from 40,000 at the end of 2011 to 31,000 by the start of 2013: we find that the remaining Financial Advisers are unduly optimistic about their own business prospects in the RDR world. However, we believe that changes in the industry have as much to do with unfolding technological and competitive forces as with RDR itself; indeed, RDR is only part of the story of change.

ii. We believe that advisers substantially underestimate the threat from D2C offerings, and are overoptimistic about future revenues from unchanging or slowly changing business models and loyal customers.

iii. Yet an increasingly financially literate, richer and computer savvy clientele will offer fertile opportunities for those advisers who can demonstrate more rigorous and sophisticated propositions going forward. The surviving advisers who rise to meet this challenge are likely to be highly qualified and can expect a buoyant demand for their services.

iv. We find that the average adviser expects to garner around £1,500 from each of roughly 150 clients to sustain the £220,000 pa of gross revenue that they tell us they require to function as a business. With fees averaging approximately 1% of assets under advisory this means that the average IFA client will need to have around £150,000 in investible assets on average. Cass research has revealed that around 1.43m people in the UK have investible assets greater than £100,000, and that just over 0.85m have investible assets over £150,000.

    If they do require around £150,000 per client then on average each IFA can expect only just under 30 clients. However, if IFAs can survive with clients possessing at least £100,000 of investible assets each, then this implies 48 clients on average for each of the 30,000 remaining IFAs. Either way these figures are far lower than the 'required' numbers indicated in our survey. This excessive optimism on future revenues suggests that many more advisers will have to leave the industry or accept far reduced incomes.

v. Of course the above numbers do not account either for regional variations in wealth or for the fact that the headline figure of £150,000 does not allow for the attraction to IFAs of the growth possibilities of smaller pots of wealth over the lifecycle of the client. The concentration of investible assets in London and the South-East, together with undoubted pockets of affluence nationally, therefore makes generalisations fraught with difficulty.

vi. Advisers point to RDR's raising of minimum education levels to QCF4 as a major reason for the timing of the recent reduction in adviser numbers. Those remaining are nearly all now appropriately qualified and hence further reductions for this reason alone cannot be expected, unless competence standards are raised yet again. We find that financial planning and its associated professional qualification are likely to become more important as part of the advisory industry's proposition.

vii. Apart from an increase in the minimum education standards required to remain as an adviser under RDR, advisers also saw increased regulatory and compliance costs, along with difficulties in adapting business models, as the other major reasons for the recent decline in adviser numbers. The minimum capital requirement of £20,000 from end-2013 will strain the resources of many smaller IFAs. The sharp decline in the undoubted cross subsidy from larger clients to smaller ones will be very challenging for many advisors: if the client with assets of £1mn previously paid 1% pa but now in the more transparent world will be paying only 20 or 30 basis points, then the potential for cross subsidy is massively reduced.

viii. The majority of advisers (69%) use at least one platform, with functionality and ease of use dominating cost as reasons for their choice of platform. Consolidation in the platform world is set to accelerate with the FCA 'platform policy paper' of April, 2013: with the banning of cash rebates to clients and the advent of transparent charging, larger platforms with economies of scale, are set to increase their market share.

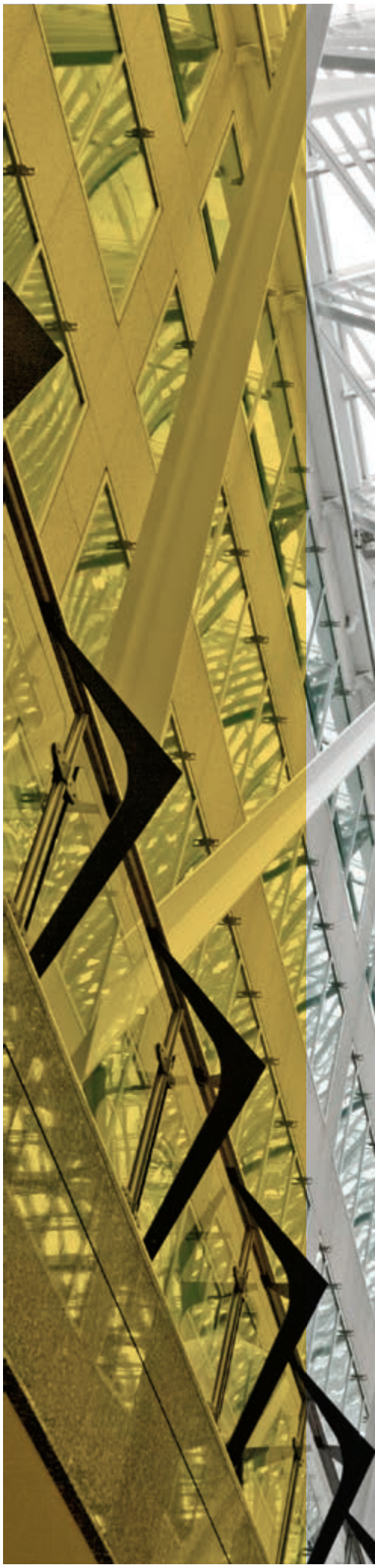
ix. IFAs see financial planning as being the major activity of the advisory community going forward. This was also reflected in interviews where the 'winners' post-RDR were often characterised as being more technically skilled and possessing of a superior client proposition.

x. 88% of advisers see value in remaining 'independent', though 58% expect to see more use made of the restricted advice model

xi. Nearly all advisers (98%) expect to charge clients at least partially on assets under advice rather than solely on the basis of a fixed or hourly fee.

xii. In valuing advisory businesses the key features mentioned by most respondents were recurring trail or fee income. Since the April 2013 announcement by the FCA of the "sunset" clause which forbids trail income from even pre-RDR sold funds from April 6th, 2016, we can expect further downward pressure on adviser revenues and business valuations. In addition, it is also possible that acquirers of advisory businesses prior to this announcement may have overpaid for these businesses.

xiii. With pressure on revenues, together with increased costs, we expect to see adviser numbers resume their downward trend once the economic realities of the new regime (driven partly by competitive change and partly by RDR and subsequent regulatory adjustments) become more visible to all concerned. This will lead to further consolidation and absorption of further books of business at diminishing prices. For the financial advisers willing to rise to these challenges, the key will be to provide a highly qualified and differentiated product proposition above and beyond the basic advice that has been sufficient in the past but which is now outmoded.



EXECUTIVE SUMMARY

The media attention greeting the introduction of RDR on 1st January, 2013 suggested that a key and failing ingredient in the UK's financial fabric was finally being kicked into touch. With the imposition of RDR a wholesome, transparent, cheaper, fairer, sophisticated (qualified to QCF4), new world of financial advice would take centre stage and transform the long-term savings' possibilities for large numbers of consumers. As part of this study our early conversations with seasoned industry professionals soon suggested that such an electrifying prospect would be unlikely in reality. With the benefit of many and varied such discussions, together with a wide-ranging industry survey, we have to admit, somewhat reluctantly, that while the morally compelling case for transparency of fees has indeed been massively advanced, business practices and structures would probably have been changing anyway, driven by technological advances and competitive forces: RDR is merely a fast overtaking dual-carriageway on the way to an already predetermined destination – it may have speeded things up, but it has probably not altered the end point. There is, of course, no definitive way of knowing what the world would have looked like if RDR had never been invented, but after only a few months into RDR(June,2013), our research also suggests strongly that some key industry features such as charging may change far less than was perhaps intended or expected.

Why do we think this ? While still early days in the RDR world, our survey finds that many IFAs believe 2014 will be another year of major changes; however, the preference for charging clients as a proportion of assets (albeit in a newly transparent way) is clearly already dominant and the idea that fee-based advice would somehow become the standard model, offering an 'objective', advisory solution is very far-fetched indeed. Sophisticated, computer- and financially-literate investors are already gravitating to internet solutions where fees are transparent and low. The awareness of ETFs, fundamental indices and similar 'economical' products is increasing exponentially.

But would these phenomena not already be well underway even if RDR had not happened? The pre-existing business model was under threat from a range of forces. On the demand side, these forces included consumers that were (are) coming to terms with unprecedented falls in real income and wealth and that are beset with a lack of trust in financial markets and institutions, and with little spare cash for savings' products. On the supply side, these forces include cheap, pseudo-advisory offerings pointing to heavily discounted passive products via the internet; an aging financial advice workforce, perhaps finding the increasingly technical and quantitative nature of financial planning and associated innovative products very challenging, and a regulator that is constantly making public noises about fees as 'destroyers of wealth', and which is constantly putting an unfavourable spotlight on certain key industry practices such as trail commission, culminating in April 2013 with the announcement that all trail commission from products sold pre-RDR will be banned. Further, along with this 'sunset' clause, the FCA stated that it would ''generally expect'' to see clients shifted into new unbundled clean share classes, which charge sharply lower annual fees to clients as they do not pay back commission to advisers or platforms in most cases.

We feel that a major shakeout of the financial advice industry was inevitable given this economic and business reality. RDR accelerated matters by putting a time-stamped floor on necessary educational qualifications which has already squeezed out many participants. Looking forward, the mismatch between the large numbers of consumers who say that they will not pay for advice and the suppliers of that advice who we find say 'business as usual' in terms of charging will be the key battleground for the future shape of the industry. Change was inevitable: RDR accelerated it.

INTRODUCTION

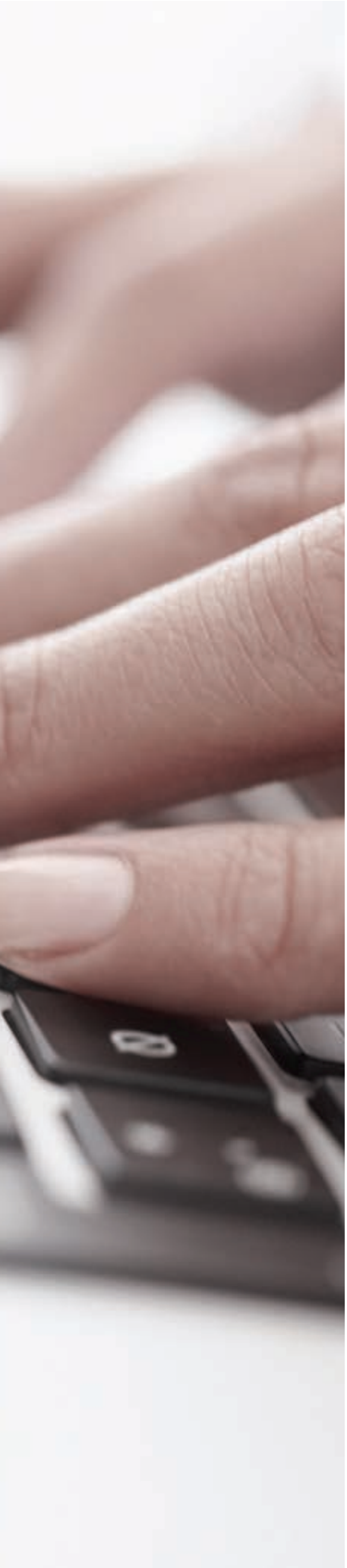
After a development period of six years, the implementation of the Retail Distribution Review (RDR) was completed on 31 December 2012. The RDR has brought in a new advisory landscape. The implementation of RDR will usher in three important changes to the financial advice landscape.

- First, depending upon the client and the type of advice sought, professional financial advisers will either charge their clients: a one-off fixed fee for advice; a fee based upon an hourly rate; a fee based upon the assets under management or under advisory; or a combination of these.

- Second, advisers will have to make it clear to their clients whether they are able to provide advice on an independent or restricted basis. Independent advisers face the challenge of providing advice which is both whole of market with regard to choice of product provider and encompasses all of the potential retail products options available to UK investors. Restricted advice may either be restricted to the products of one provider, or remain 'whole of market' but limit their advice to a restricted range of retail products.

- Finally, with the RDR the FCA hopes to improve the quality of financial advice by increasing the qualifications necessary to practise as a financial adviser.

Although RDR only came into effect from January 1st 2013, this paper reflects on the impact of the RDR on the adviser market in the UK based on in depth interviews with senior industry figures, which we have augmented with an online survey of financial advisers. This paper is one of the first to examine the consequences of this regulation on the adviser community.



In order to examine the impact of the RDR on the financial adviser community, we conducted a series of in-depth, face-to-face interviews with senior industry figures. These interviews were predominantly completed around the turn of 2012-3 and into early February 2013 and as such pre-dated the important FCA announcement in April 2013 of the banning of pre-RDR trail commission from 2016 along with the platform policy statement. The information gleaned in these interviews was crucial in helping us identify the key RDR-related issues and concerns – from the perspective of industry experts – enabling us to design an on-line survey of financial advisers. This on-line survey was sent out in early March to just over 850 UK-based financial advisers[1]. The results of the survey presented in this paper are based upon the 64 responses that we had received by March 15th 2013. Throughout the paper we draw on both the in-depth interviews and the survey to identify issues around three key themes. These relate to the impact that RDR has had, or is likely to have on:

– the market for financial advice;
– adviser business models; and
– the valuation of adviser businesses.

From recent Cass Business School research we already know that many individuals, who might have sought advice in the past where that advice was paid for via commission arrangements, will not be willing to pay fees for it in the future[2]. It would seem reasonable to assume then that the change from a predominantly commission-based model to a fee-based one will have fundamentally changed the UK's market for financial advice. But a question which is typically not asked is: would such changes have been occurring anyway through the natural evolution of competitive forces? In Section 1 of this report we focus on the advisers' views of the impact of these changes on their market. If there is likely to have been a fundamental change in the market for financial advice, it would seem equally likely that the business models of advisers will have changed, or will need to change in the future to accommodate the change in the market for advice. A business model that may have been fit for purpose in the pre-RDR world, may not be so in an RDR world. We address questions and issues surrounding adviser' business models in Section 2 of our report. Finally, there are a number of reasons why some adviser firms may not be willing to continue in the RDR world; equally there may be other adviser firms that see this as an ideal opportunity to expand their businesses. As such, there may be some advisory businesses looking for a buyer for their business on the one hand and others looking to buy these businesses. In part 3 of this report we take a look at the possible impact of RDR on the values of adviser businesses.

One of our key findings is that the advisory market is likely to become bifurcated. First, there will be face to face, bespoke advice for each individual client and secondly, there will be restricted advice, selling a limited selection of products both to those who require personal advice and a growing market with a light-touch engagement with the client. Interviewees suggest that larger IFAs may gravitate to the latter model.

1. More details of this survey are included in Appendix 1 of this paper5. Aviva Investors 2012
2. The Guidance gap report: An investigation of the UK's post RDR savings and investment landscape, A. Clare, Cass Business School, January 2013.

Although the majority of advisors in our survey expect to remain independent, 58% of financial advisers expect to see more use of a restricted model in the future. We also find that on average financial advisers expect to be able to service around 150 clients and on average estimate that they will need to earn around £1,472pa from each client to make their business models economically viable in an RDR world. This requires investable assets of around £150,000 per client on average-a number far beyond that available in practice, where 70% of the population have under £25,000 of investable assets according to a recent survey. This suggests that competition for clients with substantial assets will be fierce, including of course from Private Banks; there will inevitably be a large number of disappointed advisers who will leave the industry. Finally, we also find, unsurprisingly, that RDR is likely to have its greatest impact on smaller IFAs who do not have the necessary infrastructure to support RDR requirements, and who may be more affected by the cash-flow limiting consequences of the elimination of initial commission and the eventual reduction in recurring trail income. Our investigations lead us to the conclusion that RDR may create a greater number of willing sellers ready to sell at discounted rates in distressed sales. It also reveals that the metric most likely to be used is some multiple [around 3 times] of some definition of recurring income, which may refer to fee or trail commission, or both. It will be no surprise if this number does not fall as the end of trail commission from 2016 approaches.

Of course, even without RDR, the landscape for the advisory sector would have begun to change. Technological advances have been making the creation and delivery of investment products more accessible and cheaper to a wider audience, whether guided by an advisor or not. The growth of platforms since their introduction to the UK in 2001 has been considerable with advised platforms holding £223bn AuA as at December 2012 and non-advised, D2C platforms holding £94bn as at September 2012[3]. NMG Consulting reported in 2011 in their annual IFA survey that "68% of investors are active on at least one of the leading social networking sites". Further the widespread adverse publicity regarding fund management and advisory fees over a number of years was gradually becoming widely known among investors with the raised awareness of charging practices and the long-run wealth destruction aspects of such charges (prompted by the FCA). The global financial volatility of the last decade or so has also made investors far more sensitive to the likelihood of large drawdowns in wealth.

3. The Platforum

The industry was already shrinking pre-RDR. Since January 2006, the year the City watchdog unveiled its plans for the RDR, there were 875 sole traders. This number has fallen to 779 as at 31 December 2011. Estimates from consultancy Ernst & Young's Industry Study in 2010 predicted the number of registered individuals would fall from 30,000 to 20,000 within the five years to 2015. The number of directly authorised firms providing financial advice has fallen from a high of 5,584 in September 2008 to 5,482 at the end of 2011. The number of appointed representatives has dropped from a high of 9,372 in September 2008 to 8,590 at the end of 2011.

However, history shows that IFAs are a resolute group with predictions of a 40% fall in numbers following technological advances and the advent of stakeholder pensions a dozen years ago falling very wide of the mark. In 2006, Deloitte warned that "increased competition from areas such as bancassurance and multi-tie advisers" would put pressure on IFAs to quit. It did not happen. In the 2010 FSA policy paper they forecasted that around one quarter of advisers would leave the industry by 2012, mostly as a direct result of RDR; however they suggested that these would mostly be very small businesses and that the market would largely remain intact. This indeed seems to be the case, perhaps with the decisive, major influence being the formalisation of qualification standards. Another important influence is retirement: one IFA Census Survey by NMG Consulting in 2009 suggested that 25% of advisers would leave the advice market pre-RDR, with 6% going elsewhere in the industry, 4% leaving the industry, and 15% retiring (of which 7% would have retired anyway). RDR has certainly given the more mature advisors a reason to depart the industry.

1 THE IMPACT OF RDR ON THE MARKET FOR FINANCIAL ADVICE

1.1 RDR: GOOD OR BAD OR... ?

The RDR has been invariably described in the media and by some industry commentators as being as revolutionary, as industry changing and as redefining the financial advice landscape. But how do advisers see the RDR regime? The response of the interviewees with regard to the overall impact of the RDR on their business was rather mixed. Some viewed the new regulatory framework as being ill thought out and felt that it would have a negative impact across the industry. However, other respondents said that they had been preparing for the RDR revolution since it was first mooted in 2006 and viewed its imposition as likely to be a positive catalyst, one that would finally herald a 'proper' market for financial advice in the UK.

There was little evidence of a split in opinion on the likely impact of RDR on the mass market judging by the responses to our survey. **53% of survey respondents suggested that the mass market for financial advice would be 'less attractive' to advisers in the RDR world, while 25% said that it would make the mass market 'very unattractive'** (Figure 1.1).

Advisors who view the market as unattractive are likely to either leave the industry entirely, attempt to focus on medium to high net worth clients where providing services will become more viable, or utilise a model of restricted advice. Indeed, the overwhelming view of most of our interviewees was that the implementation of RDR would lead to a polarization and fragmentation of the advisory market. The consequence of this will be a reduction in the number of mass market IFAs, which may create a "guidance gap[4]" where many consumers may find themselves without independent financial advice, despite still having a demand for it. Although shrinking numbers of IFAs may well be one of the consequences of the full impact of this new regulation on the industry, that full impact may not be felt immediately. **Although 50% of those surveyed suggested that the major impact of the RDR would be felt in 2013, 44% suggested that 2014 would be the year when the major impact is felt** (Figure 1.2).

Figure 1.1: What impact will the RDR have on the way advisers view the mass market?

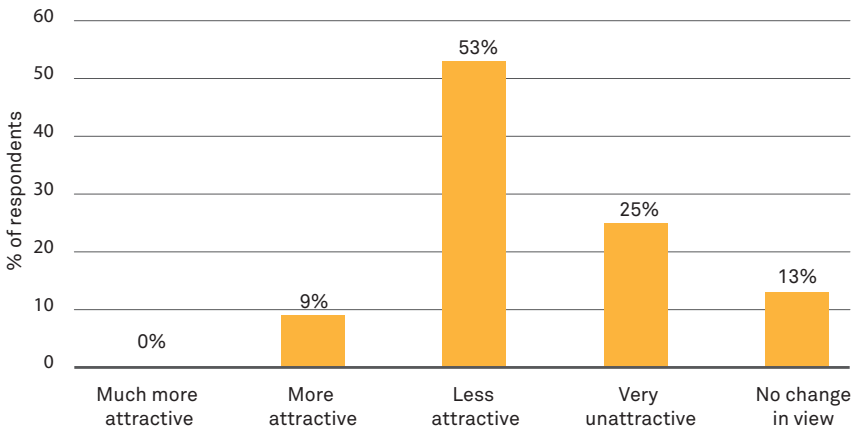


Figure 1.2: In what year do you think that the major impact of the RDR will be felt by the adviser industry?

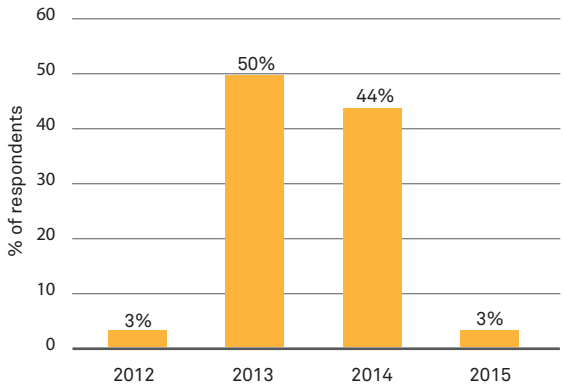
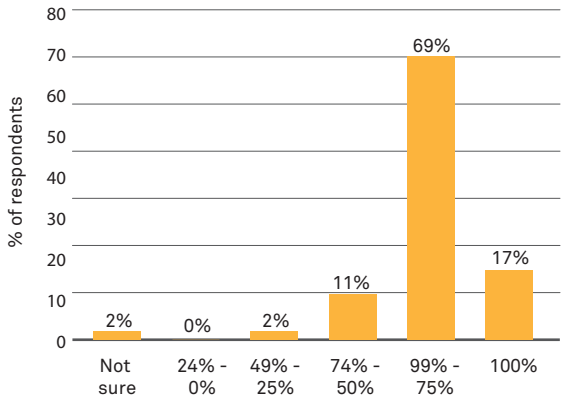


Figure 1.3: What proportion of clients do you think you will retain in the RDR environment?



Indeed, despite the concerns raised by some or our interviewees about the unattractive nature of the market for financial advice in an RDR world, 69% of the advisers in our survey suggested that they would be retaining 75% to 99% of their clients, while 17% stated that they would retain 100% of their clients (Figure 1.3). This in turn suggests that the market will go through an "evolutionary" rather than a "revolutionary" process of change, some of which may already have been underway.

1.2 THE IMPACT ON ADVISER NUMBERS

Interviewees suggested that one consequence of the RDR would be a fall in adviser numbers. It is clear that many advisors will find it difficult to make a smooth transition from a commission-based model to one based on fees, which may lead them to leave the industry. However in an important way this is possibly missing the business reality of the advisory industry which is the extent to which advisors are going to rely solely on fee-based revenue going forward? Certainly many advisors have always charged fees and will continue to do so; others will continue to charge a percentage on advised assets with little changing except the way the cash flows to them, which of course is important for transparency. In November 2012, the FSA estimated that there could be a reduction of the adviser population of around 5%. However, industry estimates of the potential decline in numbers range from around 3%[5] to close to 30%[6]. The advent of the 'sunset' clause regarding trail commission announced by the FCA in April 2013 will undoubtedly put further pressure on industry numbers.

Notwithstanding the preceding comments, there are a number of possible RDR-related factors that could drive a decline in adviser numbers. We asked our survey participants to identify these possible factors; the results are detailed in Figure 1.4. The figure shows that **47% of survey participants said that an inability to meet the minimum standard for professionalism, the QCF Level 4 qualification, would be the main reason why advisers might choose to leave the industry**. Discussions with our interviewees corroborate this view. It seems that some advisers had found it difficult to complete the exams while simultaneously running their business. However, we noted that at the other end of the scale some advisers have been able to go beyond the minimum requirements, achieving a Level 6 qualification and the status of Chartered Financial Planner. These advisers have undertaken this additional qualification in order to differentiate themselves in the market. Although there have been some discussions within the industry regarding the possibility that the 'Chartered' level would be the new industry standard, we believe that the majority of advisers will focus on maintaining their Level 4 status by complying with the related CPD requirements in the short- to medium-term, unless otherwise mandated by the FCA in the future. While the majority of advisers have understood the need to comply with the RDR-related qualification requirements, some interviewees suggested to us that some advisers might continue to advise clients without the requisite qualifications: these have been labelled 'ghost advisers' by the press. However, one would imagine that they could only do so for a relatively short period of time, before it came to the attention of the regulator.

4. The Guidance gap report: An investigation of the UK's post RDR savings and investment landscape, A. Clare, January 2013.
5. Aviva Investors 2012
6. Ernst & Young 2012

However, inability or unwillingness of advisers to achieve the professional qualifications necessary to continue to operate in the industry is by no means the only likely driver of adviser exits. Figure 1.4 also shows that a significant proportion of our survey participants felt that an inability to adapt adviser business models (36%), the increased regulatory costs associated with RDR (33%) and other regulatory requirements (34%) would also be significant factors in an adviser's to leave or to remain in the industry.

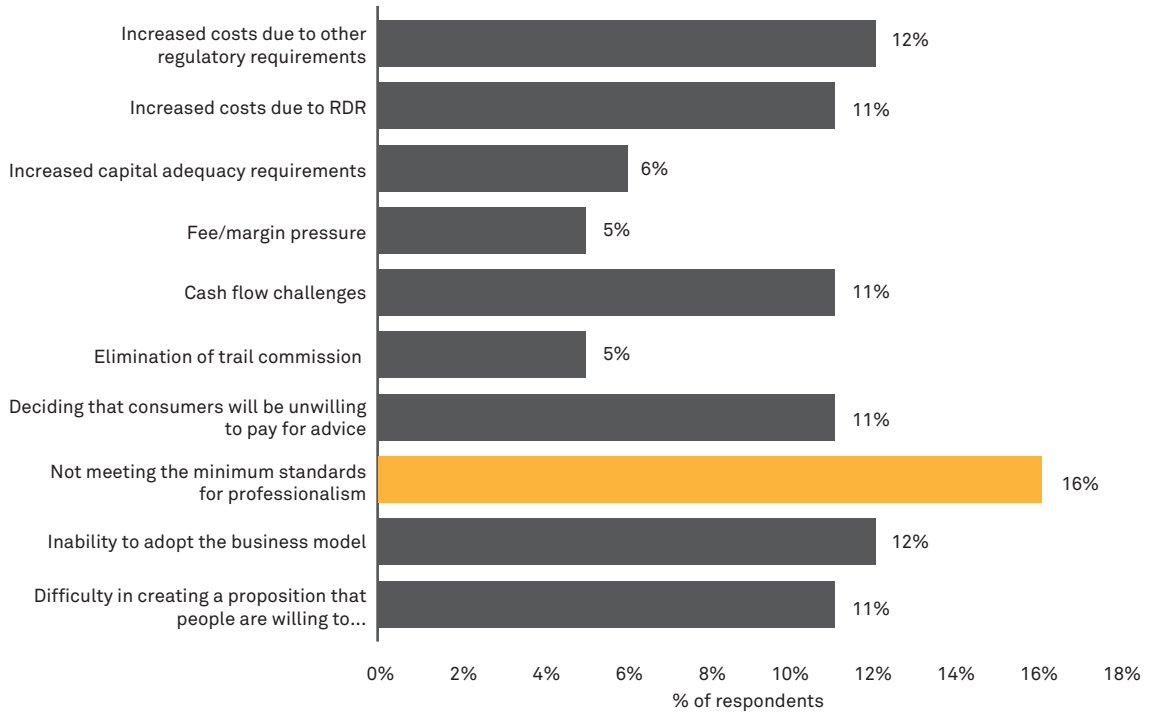
So what has been the impact on adviser numbers so far? The factors addressed in Figure 1.4 seem to have combined to create an initial 'wave' of industry exits. By the first day of RDR, the number of IFAs and tied advisers operating was 31,132, around down 25% compared with the 40,566 operating in December 2011 (FSA figures, March 28th, 2013). The first wave may well be exits related to the new qualification requirements. However, given that the overwhelming majority of those remaining are now qualified, with only a very small number close to completion or given the 30-month grace period allowed by the FCA, we would not expect this to be the main factor in any further shrinkage.

Further exits may occur as the financial requirements of running an advisory business in the future become more apparent. Our research indicates that the next 'wave' of leavers may be triggered by the difficulties that may arise from meeting the capital adequacy requirements, which are due to be implemented on 31 December 2013 after being delayed by two years to provide adequate time for advisers to change their business models. The requirements stipulate that firms should hold a minimum of £20,000, or possibly three month's expenditure; this is not an insignificant sum for a small business, particularly if revenues are already under threat from other wider, industry and RDR-related changes Further additional regulations are planned although the FCA have delayed the implementation from December 2013 to December 2015. If these new capital rules are stringent, this may precipitate a further wave of leavers.

One alternative to leaving the industry might be to join a network, which could help alleviate some of the regulatory burdens. It was suggested to us that financial advisers may be able to join a network to offset capital requirements; however 95% of the respondents to our survey were not part of a network. In joining a network, the adviser usually also obtains professional indemnity insurance (PII) as part of the package. The FCA has stipulated that independent firms need to hold insurance, which covers them for the full range of retail investment products and also hold additional capital as insurance if any products are excluded from the insurance policy. However, the increasing cost of PII will increase the cost of joining such networks.

But would there have been a drift downwards in adviser numbers regardless of RDR? Of course it is impossible to tell conclusively, but the forces mentioned in the introduction certainly suggest that this is possible.

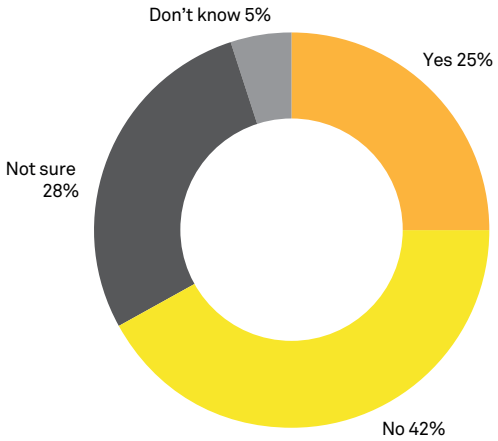
Figure 1.4: Which of the following reasons would be most likely to cause advisers to leave the industry?



1.3 THE RE-EMERGENCE OF DIRECT SALES FORCES

The imposition of the RDR has brought about a clear shift in the distribution landscape. The disappearance of the commission-based model has created a clear distinction between advice on the one hand and product providers on the other. Because of this, asset managers, life companies and other providers have sought to develop new ways to get their products to market and to regain some control over distribution. Interviewees suggested that the prospect of a decrease in adviser numbers together with an increase in 'orphaned' and low value clients may encourage big providers to launch the sort of direct sales forces that were common in the 1970s and 1980s. It was argued that these large product providers – who may have hundreds of thousands of small, low value policy holders of their investment products – would effectively utilise sales teams to target low value or orphaned clients by offering a restricted service with a limited range of products while charging a RDR-compliant fee. Indeed, 2012 saw the re-launch of direct sales force teams from providers such as Prudential. However, despite the reported prospects of a resurgence in this area, 42% of our survey respondents suggested that there would not be substantial growth in direct sales forces (Figure 1.5), although 25% said that there would be, while 28% indicated that they were not sure. While initially puzzling given the high profile announcement regarding these initiatives, it is entirely consistent with advisers believing that they will hang on to their existing clients (see Figure 1.3 above). Although the re-emergence of direct sales across the wider industry is still at an early stage ,we believe that **the economics of launching (or re-launching) a direct sales force for large providers is potentially so compelling that financial advisers may well have underestimated the potential threat that such growth could pose for their businesses. Furthermore, and perhaps of more importance, a significant growth in direct sales forces would seem to be counter to everything the FCA have been trying to achieve with RDR.**

Figure 1.5: Do you think that there will be a substantial growth in Direct Sales Forces?



1.4 PLATFORMS IN AN RDR WORLD

The growth of advised platforms, where the adviser interacts with the platform on behalf of the client, has been phenomenal in recent years. In Q1 of 2012 the total amount of advised assets on platforms was £190.3 billion, this figure represented growth of 7.9% over the previous quarter[7]. As at December 2012, the assets under advice on platforms had reached £223bn[8]. Our survey was conducted before the long awaited FCA's 'platform policy statement' of April 2013 but still reveals some relevant and interesting features. We asked our survey respondents about the importance of platforms for their businesses: **69% of respondents confirmed that they will use multiple advised platforms in their business while 27% said that they would have one primary platform** (Figure 1.6). Only 3% of respondents said that they would not use a platform. These results underline what an important component of the financial advice landscape platforms have become. Advisers find platforms to be of benefit because they provide an aggregated view of client' assets and the performance of these assets across the adviser's client base. Platforms also help to reduce the paperwork and administration of an adviser's business. Yet these forces have been at work for some time. Technology and cost improvements have made it easier for advisers to service clients in a cost-effective way, and given the often-heard comments about the difficulty of achieving consistent profitability for platform operators it would be reasonable to assume that any surplus generated has gone to the adviser community. RDR has not really interfered with this progress, though the FCA's platform policy statement of April,2013, promises to lead to significant changes in this area (see below).

Given that platforms appear to constitute such an important part of the financial advice landscape, we were keen to understand what platform features are valued most by advisers. **In considering the choice of a platform, 46% of advisers were focusing on the functionality available, indicating that ease of use ranks relatively highly for advisers** (Figure 1.7). Interestingly only 20% of our respondents ranked cost as the most important factor in choosing a platform.

How could the recent FCA platform policy paper impact these issues? Under these rules, product providers are banned from providing cash rebates to platforms from April, 2014,and from April, 2016 platforms will have to ensure that they apply a "platform charge" to customers, for both new and legacy business: platforms must make the cost of their services clear to investors with a fully disclosed and transparent charge. This also applies to non-advised platforms. These rules are intended to improve transparency for investors and restrict the influence of product providers and platforms on the promotion of one fund over another and are in line with RDR in ensuring that cash rebates cannot be used to offset charges for advice. This will inevitably accelerate the move to clean share classes and platforms will want to negotiate deals with product providers for individual discounted share classes, which in itself could prove a costly process if multiple share classes have to be created for the same fund. The sunset clause for rebates will also accelerate this process. It is widely thought that this will increase the pace of platform consolidation as the larger ones seek to use their scale and efficiency to secure better terms from fund managers, though the existence of multiple share classes will make migration across platforms more complex.

Figure 1.6: What is your view of the importance of platforms for your business in the future?

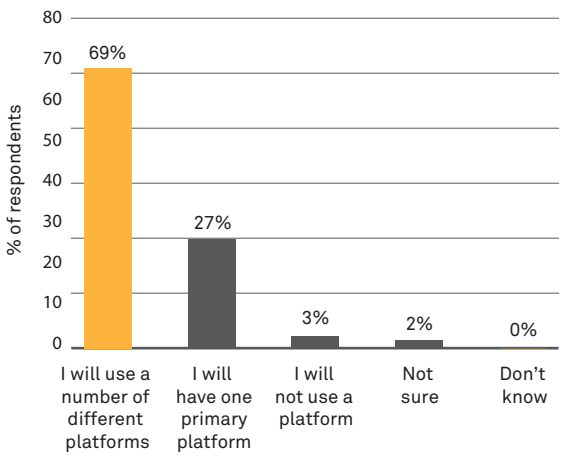
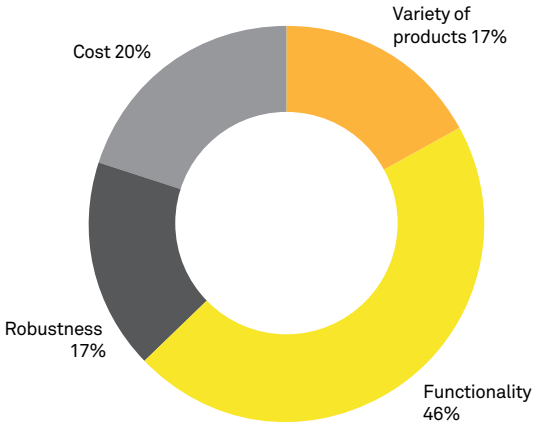


Figure 1.7: Which one of the following factors is most important to you when selecting a platform?



These results indicate that the likely platform winners in a RDR world will not necessarily be the cheapest, but instead the ones that offer the best functionality, functionality that presumably continue to improve with ongoing technology advances. However, it seems very likely to us that this would have happened anyway, even without RDR. And indeed, the April,2013 paper by the FCA on platform charging will only accelerate consolidation in the sector, with the larger platforms likely to be the winners as transparent costing will favour their lower average costs which go together with scale. Cost is likely to emerge as the most significant factor going forward.

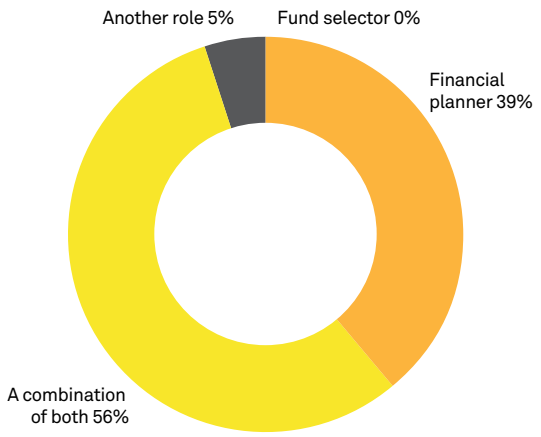
1.5 THE ROLE OF THE IFA IN A RDR WORLD

In the past financial advisers may have been seen as being the "fund selectors" in the distribution process. However, the arrival of RDR and the related fee-based advisory model, has now effectively separated the cost of investment products from the cost of their distribution. An interesting question is whether this has happened in practice.

Consumers and their financial advisers now sit on the same side of the table. This in turn means that the role of financial advisers may also be changing from the role of "fund selector" in the distribution process to one of "financial planner". Indeed, our interviewees suggested that the traditional 'IFA' label would become redundant in time as the focus of the role changes. We asked our survey participants for their views of the future role of the "IFA". These results are presented in Figure 1.8. Only 5% of respondents saw the role as being predominantly that of a fund selector, while 39% viewed the primary future role as that of a financial planner. However, the majority of our respondents (56%) suggested that the primary role would be a combination of fund selector and financial planner.

However, perhaps the biggest challenge facing IFAs as they try to redefine their role in a RDR world will come from web-based services. Our interviewees indicated that these services could represent a particular challenge to those advisers that had a large pre-RDR base of "low value" clients. But such technological innovations were well in place pre-RDR and in an increasingly computer literate

Figure 1.8: What do you see as the primary role of the IFA in the future?



society one would expect a greater willingness by clients across the wealth spectrum to bypass advisers with DIY investing. Indeed, earlier research by Cass has already identified that a significant proportion of the UK's population would be willing to use a "financial guidance service" instead of using a financial adviser to help them make their savings and investment decisions. These non-advised or direct-to-consumer (D2C) platforms consist of either IFA branded platforms, fund manager-owned platforms or execution-only stockbroker platforms. Today this non-advised technology is accessed directly by over 6.5 million private investors in the UK. Hargreaves Lansdowne and Fidelity are two of the best known such offerings. The D2C platform market had £94.3 billion in assets under administration as at September 2012 . The growth of these platforms could continue to represent a considerable shift in the source of financial advice sought by consumers, given that the Cass research indicated that just over 26 million UK adults would not be willing to pay for financial advice. **However, despite the obvious challenge of these D2C websites our survey revealed that only 9% of our respondents viewed them as a threat to their business. Again we feel that they may have underestimated at least the long-term threat of such services to their businesses.**

7. The Platforum, 2012
8. The Platforum, 2013

1.6 CONCLUSIONS

The results of our surveys, interviews and our own analysis have led us to the conclusions that RDR will tend to favour stronger, more process-focussed firms of financial advisers. It seems likely to us that these firms will not only survive in the RDR world, but will also prosper from the new regulatory environment as overall adviser numbers decline and as they focus on higher value clients that may have become advice orphans or that that may have been traditionally serviced by wealth management companies. This would also mean, of course, that firms of small advisers, the 'cottage industry' component of the financial advice industry, will shrink.

Beyond this change we find evidence to suggest that the market for financial advice will probably become bifurcated. On the one hand there will be face to face, bespoke advice for individual clients; while on the other there will be growth in restricted advice selling a limited selection of products with a light-touch engagement with the client. The restricted model may well turn out to be driven predominantly by the re-emergence of the direct sales forces of large product providers as they look to regain control of their distribution channels, though we do not see much evidence of this yet. If it does happen in the near to medium term, then the re-emergence of direct sales forces is presumably an unintended consequence of the RDR changes, although it is interesting to note that advisers do not view the growth of this to be a threat to their business. Interviewees also suggested that larger IFAs may also gravitate to the restricted advice model. Although the majority of advisors in our survey expect to remain independent, 58% of advisers believe that more IFAs will utilise a restricted model in the future. Many advisers will not have the resources or time to provide whole-of-market advice and therefore will choose to limit the products on offer to clients.

But a key question which has not been addressed by many, if any, commentators on the impact on the industry for financial advice, is whether many of these changes might have been happening anyway?

Certainly it seems likely to us, for example, that the popularity of D2C, web-based services such as Hargreaves or Fidelity would have continued to grow and to threaten the business models of advisers focussing more on the mass market for advice anyway. As such, although RDR has clearly driven the professionalisation of the advice industry through raised qualification requirements, the technological developments that we have seen recently, and the growing demand for transparency amongst consumers may well have continued to change the industry in a way that would have been consistent with the FCA's aims, even in the absence of RDR.

2. THE IMPACT OF RDR ON ADVISOR BUSINESS MODELS

The change from a predominantly commission-based to a fee-based advisory model, clearly means that the business models of many advisory firms could be quite different. For example, we can expect large clients to be less likely to cross-subsidise advisers' services to smaller clients in the future, thus there will be a greater segmentation of clients. To some extent the business models will have to adapt to the behaviour of consumers of financial advice. Many mass market, and even many mass affluent and high net worth individuals may be content to utilise non-advised, self-service platforms, whereas others will require the sort of advice typically provided by a financial adviser. For those firms that opt to remain independent, it will be vitally important that they have a clearly structured client proposition and that they can demonstrate clearly the ways in which they will add value to a client's financial health compared with non-advice providers. In this section of the paper we look at the likely changes to adviser business models as a result of the changing landscape brought about by the RDR.

2.1 INDEPENDENT V RESTRICTED

A key decision for financial advisers is whether they should operate under an independent model or whether to offer a restricted service. It has been widely predicted that RDR will lead to an increase in the provision of restricted financial advice due to the considerable commitment that would be involved in providing the alternative "whole of market" service. Despite this potential issue, **88% of survey respondents said that they would provide financial advice using an independent business model post-RDR** (Figure 2.1). This result indicates that advisers clearly see considerable value in the provision of independent advice in the retail investment industry – or at least that they perceive that their clients will value such a service. Retaining the independent label will be advantageous because the adviser will be able to cater for the majority of clients, and this may encourage referrals to bring in more high net worth individuals. However, these benefits need to be weighed up carefully against the cost of achieving compliance in the RDR world.

However, our survey also showed that 58% of IFAs believe that there will be greater utilisation of a restricted model in the future (Figure 2.2), citing a lack of resources and the need to reduce costs as the main potential reasons for choosing this model (Figure 2.3).

Restricted advice has to meet the same standards for suitability, charging and professional standards as independent advice with any restrictions disclosed in writing and reviewed in person with the client. In addition, the knowledge gap between those offering restricted and independent financial advice may not be as large as originally thought because restricted advisers will also need to document why a particular product was not included in the analysis for the client. This means that whole of market knowledge will be required, even for restricted advisers.

Figure 2.1: What business model will you employ in the RDR world?

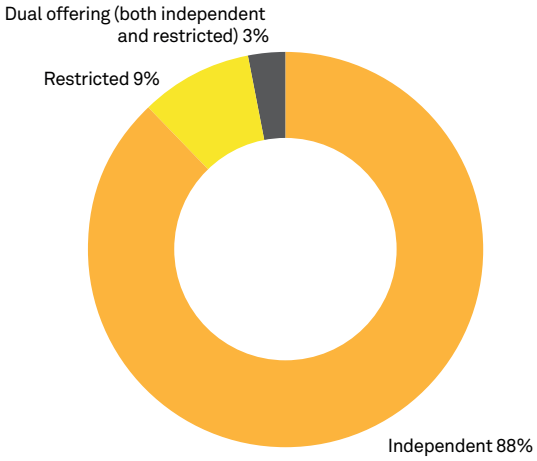


Figure 2.2: Do you think that IFAs will make more use of a restricted business model in the RDR world?

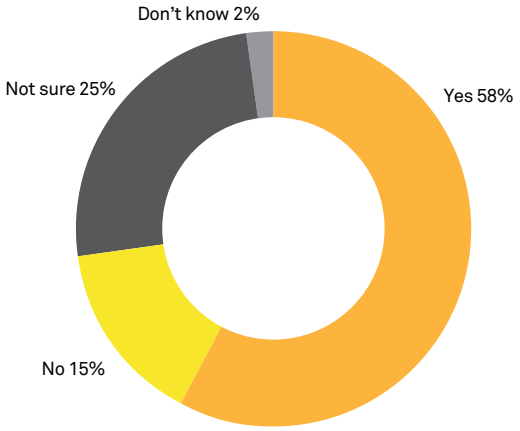
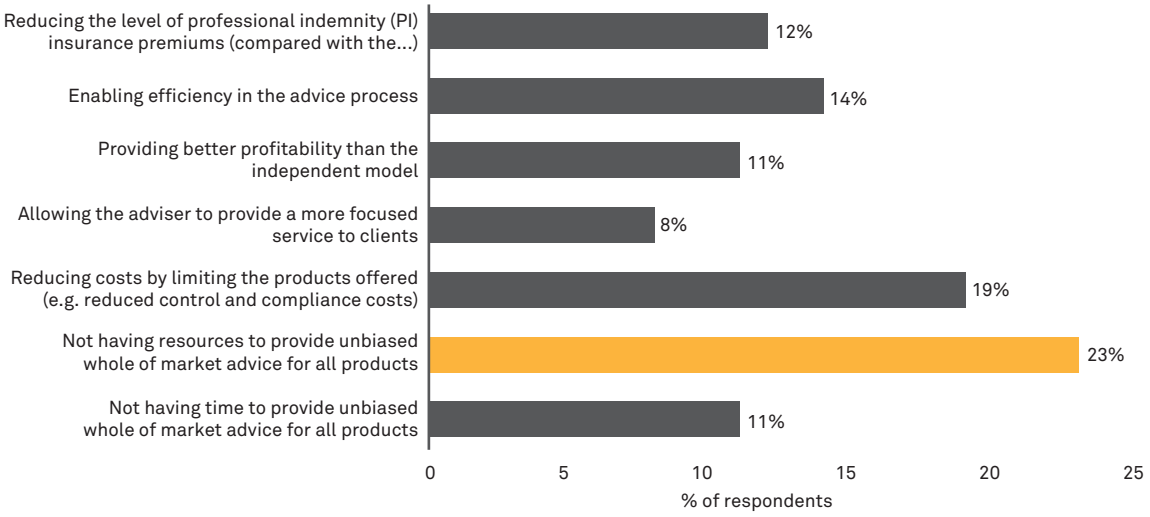


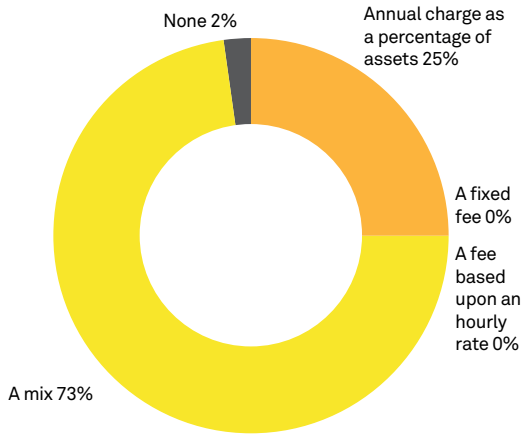
Figure 2.3: What do you think the main reasons are for using a restricted business model?



2.2 FEE STRUCTURE

The largest change to business models will be the propagation of adviser charging and the elimination of commission-based selling. Indeed the latter will be banned completely for both new and pre-RDR business from 2016(the so-called 'sunset' clause). Advisers who have previously relied on provider commissions will need to be able to adjust to the concept of remuneration via the client. This will effectively eliminate the opportunity to cross-subsidise from bigger clients to support smaller clients and the offering to each client will need to be considered with this in mind: client segmentation will increase. Although 25% of our respondents indicated that they will be charging a fee based upon percentage of assets under advice, **73% of respondents to our survey stated that they would be using a mix of fee types, utilising an annual charge as a percentage of assets, a fixed fee and/or a fee based upon an hourly rate** (Figure 2.4). Many advisers have been charging fees for a number of years prior to RDR; however, IFAs who were previously commission-based will need to adjust to a setting where their fee will now have to be agreed with the client before any advice or before any sale can take place.

Figure 2.4: What fee structure will you be using in the RDR world?



Cost will become a key factor in the relationship between the adviser and the client. Advisers in our sample had a broadly positive view regarding the change to remuneration via an explicit fee. 31% of our respondents told us that 100% of their clients would be willing to pay a fee-based charge, while almost half of the respondents (48%) suggested that at least 75%-99% of clients would be willing to pay (Figure 2.5). In addition, 83% of advisers in our survey remain confident that the fee-based charging will become more accepted by clients over time (Figure 2.6). We question whether this really is likely,especially given the additional transparency issue and perceived increase in the cost of using platforms which will be soon be introduced.

Figure 2.5: What proportion of your clients do you think will be willing to pay the fee-based charging required by the RDR?

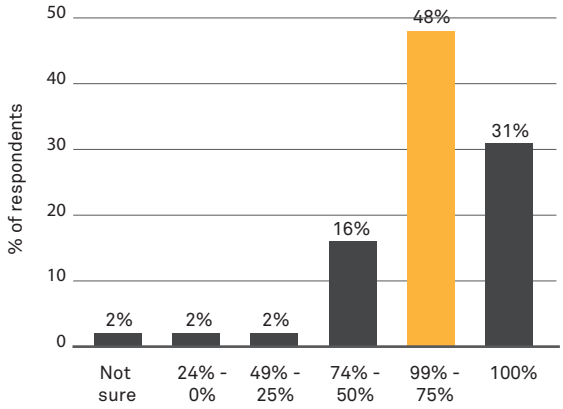
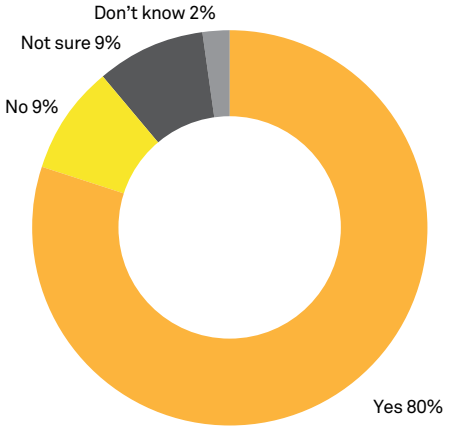


Figure 2.6: Do you anticipate greater acceptance by clients of the fee-based remuneration structure over time?



2.3 CLIENT SEGMENTATION

The advent of RDR will further increase the number of advisers actively segmenting their client bases. Any segmentation will clearly be determined by the level of service that clients will be offered which, in turn, will be influenced by the potential profitability of each client. We asked advisers to confirm how they analysed their client base, as a function of the following attributes: the complexity of the client's circumstances; the willingness or ability to pay fees; the client's own knowledge or sophistication of products; and the quantity of assets under management or advice. **86% of our respondents said that they had segmented their clients on the basis of assets under management or advice** (Figure 2.8). This is because this metric is frequently used to calculate the revenue that can be earned from a client. However, a significant proportion (33%) said that they had segmented their clients based on the complexity of a their clients' circumstances; although it may be that wealthier clients tend to have more complex financial circumstances, so that this too could be a proxy for asset under management.

Figure 2.7: Have you segmented your clients since the advent of the RDR?

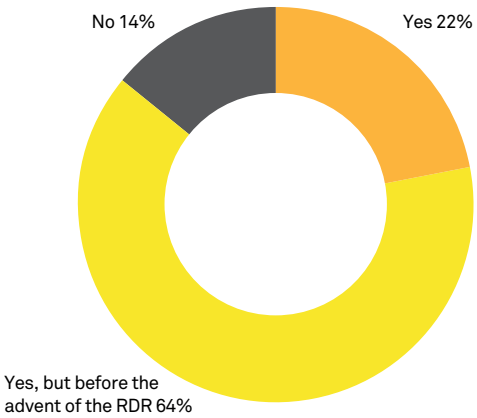
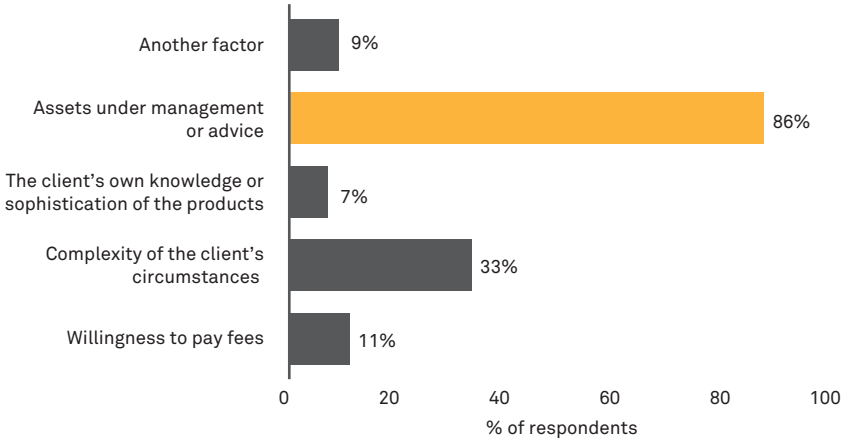


Figure 2.8: How have you segmented your clients?



2.4 BUSINESS MODEL READINESS

So how prepared were financial advice businesses for the RDR revolution? **When we asked when their business model would be ready for RDR, 86% of our survey respondents indicated that it already was ready** (Figure 2.9). 12% said that it would be ready within 12 months, while only 2% said that it would be ready within 24 months. The fact that such a high proportion of businesses are already prepared, or are nearly ready for RDR, should not come as a great surprise given the gestation period of this set of regulations.

Given that RDR will dramatically alter the way that many advisers are remunerated we felt that it was important ascertain what advisers believed would be a sustainable economic business model. First, we asked advisers how many clients they felt that they could service properly.34% of respondents suggested that they could meet the needs of 'more than 125' clients; while 31% of respondents suggested that they could properly service between 101 and 125 clients (Figure 2.10). Our survey results indicate that advisers believe that on average an adviser could service 150 clients. Next we asked what annual revenue an adviser would need to generate on average from their clients. 41% of respondents suggest that they would need to earn £1,001 to £2,000 per client in order to make their business viable (Figure 2.11).

From our survey results we estimate that advisers believe that the average revenue that they need to generate per client to make their businesses viable is around £1,500. We find that the average adviser expects to garner around £1,500 from each of roughly 150 clients to sustain the £220,000 pa of gross revenue that they tell us they require to function as a business. With fees averaging approximately 1% of assets under advisory this means that the average IFA client will need to have around £150,000 in investible assets on average. Cass research has revealed that around 1.43m people in the UK have investible assets greater than £100,000, and that just over 0.85m have investible assets over £150,000.

If they do require around £150,000 per client then on average each IFA can expect only just under 30 clients. However, if IFAs can survive with clients possessing at least £100,000 of investible assets each, then this implies 48 clients on average for each of the 30,000 remaining IFAs. Either way these figures are far lower than the 'required' numbers indicated in our survey, with advisers thinking that they will need 150 clients each with assets of about £150,000.

But are there enough clients to support this revenue stream? We think not. Of course this does not drill down to the profound regional variations which will occur in the distribution in investible assets or the fact that someone with much less than £150,000

Figure 2.9: When will your business model be in the correct state for the RDR world?

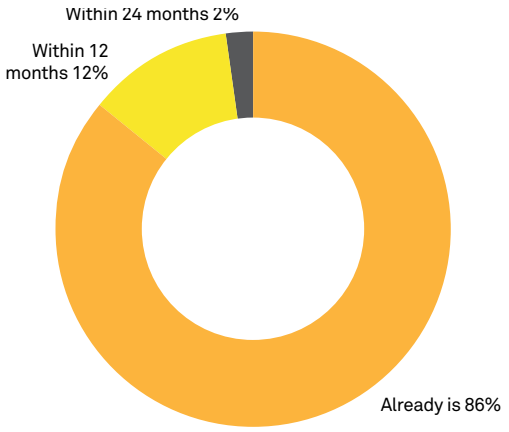
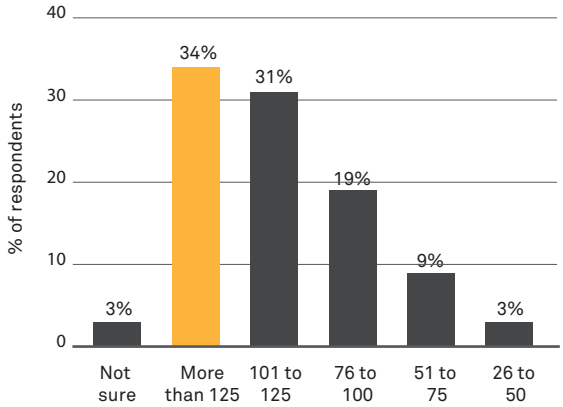


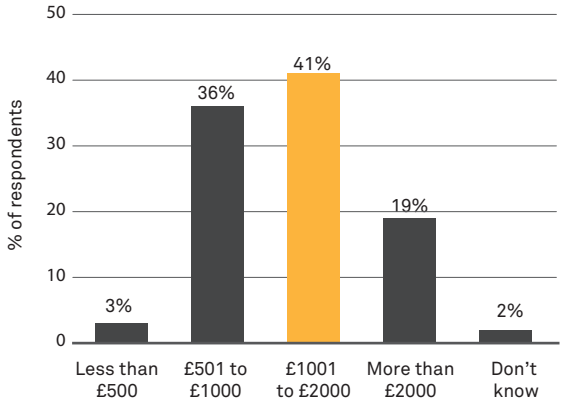
Figure 2.10: How many clients do you think an adviser will be able to service properly in the RDR world?



in assets may be seen as a good long-run potential client as wealth is expected to grow. But this excessive optimism on future revenues suggests that many more advisers will have to leave the industry or accept far reduced incomes.

These results indicate, indirectly, that advisers will target the mass affluent to high net worth individuals in order to generate enough revenue to support a sustainable business in the RDR world and, in addition, that they will adapt their client propositions to provide a broader and more sophisticated range of products to support this approach.

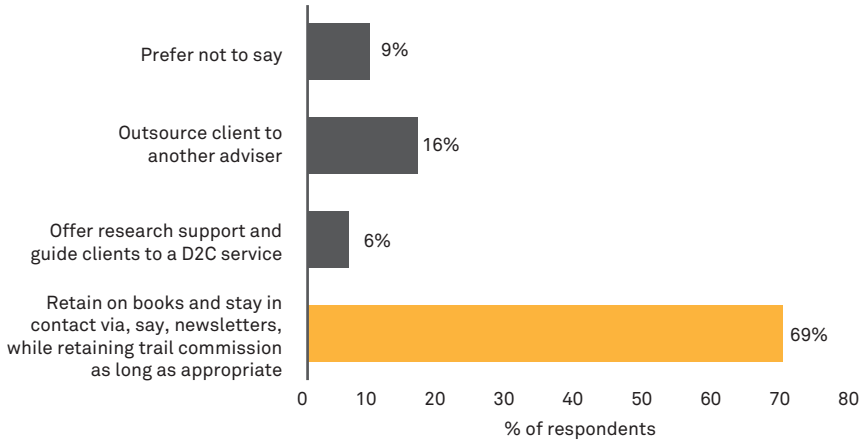
Figure 2.11: Approximately what average annual revenue do you think you will need to earn from a client to make your business commercially viable?



Of course, if some clients are commercially viable (those with quite significant investible assets) then there will be others that will not be. When asked what they proposed to do with clients that would not be commercially viable in a RDR environment, 69% of advisers suggested that these clients would be maintained on the books in order to maintain trail(which we now know, of course, will end from 2016), but that they would not receive the full service (Figure 2.12). Instead these clients would receive correspondence or newsletter service via e-mail; clearly this is a negative outcome for the client. Interestingly, 16% of respondents suggested that they would outsource these clients to another adviser. However, it is not entirely obvious why a client would be economically unviable for one adviser but viable for another. However with the demise of all trail commission from 2016 these comments may already be both over optimistic and out-of-date.

Overall, our results indicate that one of the unintended consequences of the RDR – perhaps the most important unintended consequence – will be that the mass market for financial advice is even less likely to be provided for in a RDR world than they were before its implementation.

Figure 2.12: How will you manage clients that are no longer commercially viable to receive your full service?

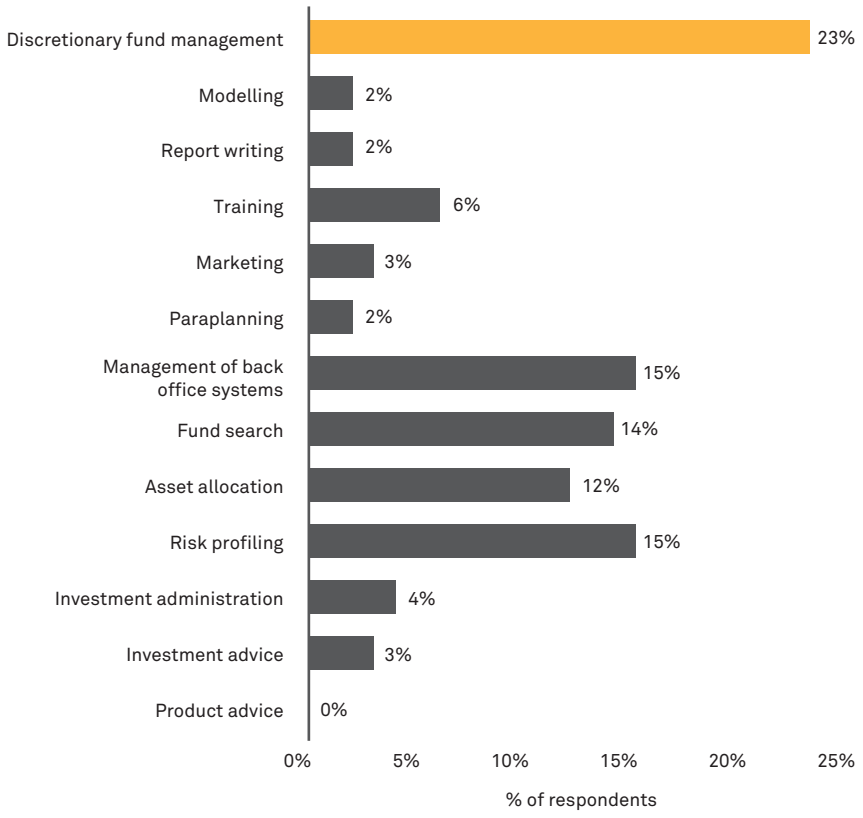


2.5 OUTSOURCING

Finally, a number of industry commentators and some of our interviewees have suggested that outsourcing arrangements will increase in the RDR world as advisers look to reduce the cost of compliance. Despite this, **91% of the respondents to our survey said that they have not increased their use of outsourcing arrangements as a result of RDR.** However, these are still early days, and this figure may change as the full consequences and effects of RDR are felt. For those that do outsource services, discretionary fund management (DFM) is by far the main outsourced service (Figure 2.13).

The DFM services can be divided into either bespoke, managed portfolios or into unitised funds; which service is most suitable for a client is the responsibility of the adviser for the unitised funds, and is shared between the adviser and DFM for the former options. DFMs are competing for assets and therefore subject to pricing pressure, resulting in lower costs for these services. Therefore when considering outsourcing, advisers are increasingly looking to delegate their investment management process via the use of DFMs.

Figure 2.13: Which services do you currently outsource?



2.6 CONCLUSIONS

The change from a predominantly commission-based to a fee-based advisory model, clearly means that the business models of many advisory firms could be quite different. So what will a typical advisory business look like in the RDR world? The majority intend to offer an independent business model post-RDR where fees will generally be based upon a mix of an annual charge as a percentage of assets, plus a fixed fee and/or a fee based upon an hourly rate. This precise mix of fees for any individual client will depend upon which segment of the advisers client base that they fall into. The vast majority of advisers have already, or intend to, segment their client bases. Finally, the all important question: what gross revenue will make advisory businesses sustainable? Our research indicates that average gross annual revenue of around £220,000 per adviser will be needed to make their business models sustainable in a RDR world.

So if the average adviser expects to garner around £1,500 (£220,000/150) from each of roughly 150 clients to sustain the £220,000 pa that they tell us they require to function as a business, with fees averaging approximately 1% of assets under advisory this means that the average IFA client will need to have around £150,000 in investible assets on average. As we noted, Cass research has revealed that around 1.43m people in the UK have investible assets greater than £100,000, and that just over 0.85m have investible assets over £150,000. If they do require around £150,000 per client then on average each IFA can expect only 30 clients. However, if IFAs can survive with clients possessing at least £100,000 of investible assets each then this implies 48 clients on average for each of the 30,000 remaining IFAs. Either way these figures are far lower than the 'required' numbers indicated in our survey, with advisers thinking that they will need 150 clients each with assets of about £150,000.

This excessive optimism on future revenues suggests that many more advisers will have to leave the industry or accept far reduced incomes. Taking all this together, including the segmentation of client bases and the revenue targets, our results indicate that one of the unintended consequences of the RDR – perhaps the most important unintended consequence – will be that the mass market for financial advice is even less likely to be provided for in a RDR world than they was the case before its implementation.

3. THE IMPACT OF RDR ON THE VALUE OF ADVISORY BUSINESS

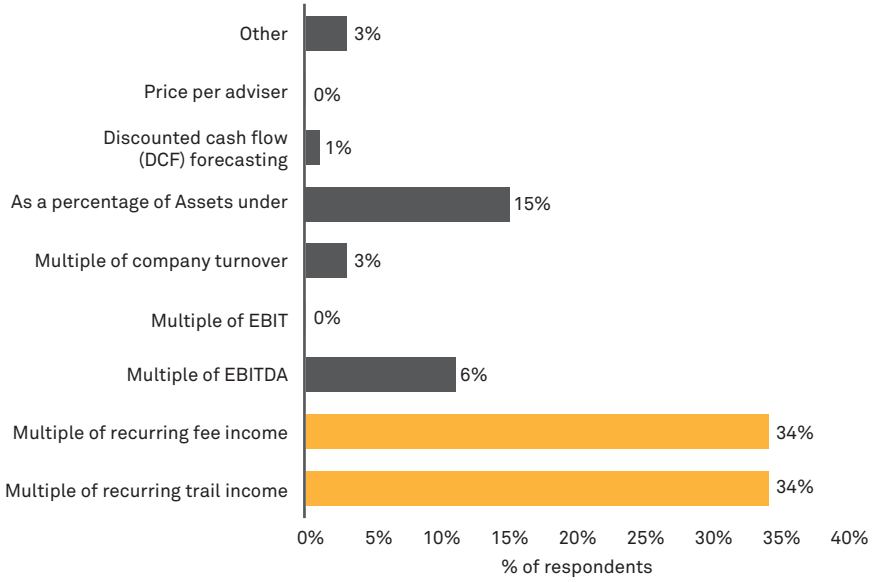
Our interviewees and other research has revealed that there is a strong belief in the industry that advisor numbers will shrink. Those that feel, for whatever reason, that they do not wish to work as a financial adviser in the RDR world will therefore naturally seek to capitalise the value of their business via an industry sale if they can. During the interviews that we conducted and via the on-line survey(which both pre-dated the FCA papers announcing the complete end to trail commission from 2016 and the platform policy statement) we investigated the issues around the value of advisory businesses and the possible impact that RDR might have on these values. Anecdotal evidence and feedback from interviewees suggests that in the run up to the implementation of RDR, **there were greater levels of distressed sales of mainly smaller IFA businesses.** These smaller firms have decided to leave the industry.

3.1 FINDING VALUE IN AN ADVISORY BUSINESS

The value of an advisory business will depend on a number of interrelated tangible and intangible factors, which make the challenge of arriving at an appropriate value difficult. For example, it might be reasonable to assume that the value might be influenced by the level of recurring income; the number and experience of the business's advisers; the quality of the client bank; the systems and IT; and brand presence. **However, of all of these factors our interviewees suggested that the quality of the client bank would be the most important consideration when purchasing a business.** In addition, they suggested that the IT infrastructure and systems of the business might not be so important as long as assets could be transferred easily to the platform of the purchaser.

For researchers trying to understand the value of an advisory business the issue is complicated by the wide range of valuation metrics in use across the industry. Current metrics include variants of multiples of income, profitability and turnover as well as a consideration of assets under advice or management. Our interviewees conceded that in reality, no one metric would be likely to encapsulate the complete picture of value and therefore that acquirers and sellers were likely to negotiate a price possibly as a function of a combination of measures. This view is also borne out by the respondents to our on-line survey. We asked respondents to identify for us the main valuation metric. **34% of the responses confirmed that the main metrics utilised are based on multiple of recurring trail income or the multiple of recurring fee income** (Figure 3.1). However, it seems likely to us that the use of the former metric will decline as trail commission gradually comes to an end, and indeed will reduce even more quickly now that the 'sunset' clause has been announced. The survey respondents also indicated that two other metrics were common: profitability, expressed as a multiple of EBITDA; and based upon assets, expressed as a percentage of assets under management or advice.

Figure 3.1: From your experience, what is the main valuation metric used in the sale of advisory businesses?



3.2 VALUATION PRIOR TO RDR

In 2012, interviewees and industry sources suggested that valuations of advisory businesses averaged between 2.5x to 3.0x recurring income. Higher multiples of 3.5x to 4.0x were achieved for smaller IFA sales, depending on the constituents of the business. Our interviewees explained to us that the multiple valuation is usually driven by profit in the business at deal completion and the opportunity for increased profit post deal completion. When acquirers look to buy businesses, they are generally interested in firms where there is the potential to increase advisory fees and where there is a prospect of reducing the payments to any discretionary fund manager or platform that the firm might use so that the total expense ratio can be improved. If the acquirer actively manages funds, they may increase charges for asset allocation and underlying fund management in addition to advice, thereby further enhancing the post-deal value.

3.3 VALUATION IN A RDR WORLD

We asked advisers about the likely trends in valuations that might arise in a RDR world. Although a number of interviewees suggested that there would be either no change or that it was 'too early to tell', **44% of advisers in our survey suggested that there would be lower valuations in the next couple of years** (Figure 3.2). If this view was common in 2012, it perhaps explains the wave of sales in that year. This may be because transactions involve largely buying the client bank and achieving revenue via the recurring trail. But we now know that trail will not continue beyond April 2016. Therefore peak trail is likely to have occurred on 1st January 2013 and will decline from this point. Valuations must now decline.

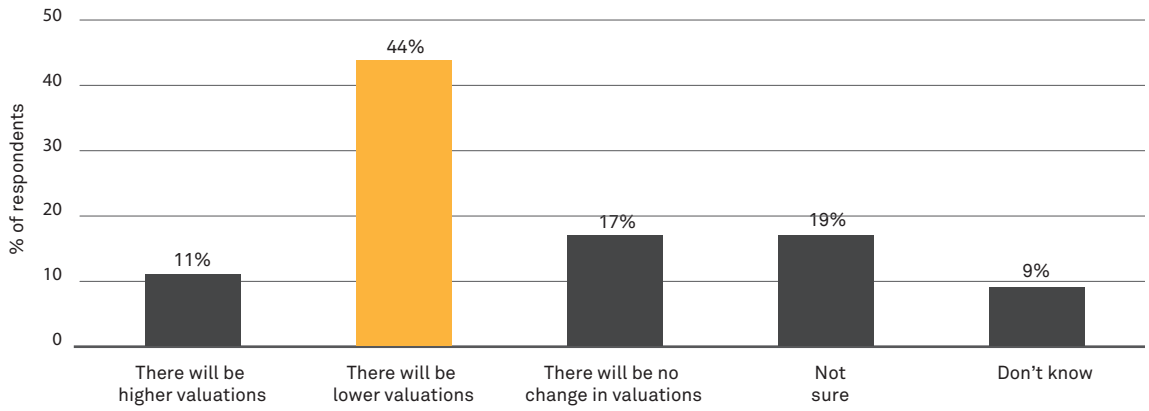
The gradual diminution of trail commission even up to 2016 will mean that other factors will eventually become the principal drivers of valuation. For example, it is likely that the level of income derived from a fee-based ongoing service will become an important constituent of valuation. In addition, Ernst & Young have suggested that a track record of transparent adviser fees being paid by clients will become important although this metric will only be visible some months after the commencement of the RDR regulations.

17% of respondents suggested that there will be higher valuations in the future. A number of interviewees suggested that there would also be longer tails for pay-outs. This view may have been driven by an alternative approach to transactions where the trail was maintained with the original owners of the business. In this "partnership model" a new firm may provide services in exchange for acquisition of the client list of another firm, but the trail would have remained with the original firm. **Thus the maintenance of the trail commissions would have increased the value of the business with this transaction model quite dramatically, compared to one which could cause the trail to decline sharply after the sale. Of course, this will change now with the publication of the 'sunset clause' regarding trail.**

Finally, respondents to our on-line survey also suggested that there would be a **wide range of approaches to valuation in the sale of advisory businesses.** These ranges would include trail income multiples ranging between 1.0x and 7.0x; 1.0% to 4.0% of assets under advice/management; 1.0x to 4.0x recurring fee income; 1.5x to 3.0x of turnover; and combinations of trail and EBITDA multiples.

Overall there seems to be great uncertainty about how a financial advisory business will or should be valued, and that the value could change dramatically depending upon the transaction model. **Furthermore, with the recent announcement by the FCA of the "sunset" clause which forbids trail income from even pre-RDR sold funds from April 6th, 2016, we can expect further downward pressure on adviser revenues and business valuations going forward. In addition, it is also possible that acquirers of advisory businesses prior to this announcement may have overpaid for these businesses.**

Figure 3.2: What is your view of trends in valuations of advisory businesses in the next 1-2 years?



3.4 THE ROLE OF CONSOLIDATORS

Interviewees had mixed views about the role of consolidators in the market place. Some said that consolidators would be simply "mopping up AuM" and "flipping themselves into advisers" and were therefore likely to provide a poor service to clients. However, others suggested that the latter types of firms would not survive in the longer term and that the better consolidators were providing a useful service to the industry, playing a key role in supporting the migration of clients to new services. As was suggested in earlier research, the IFA brand may be changing but as well as a change in the role of the adviser, the RDR world may better support structured, larger IFA businesses offering restricted advice, such as those that are set up as consolidators.

The increase in consolidator activity in the run up to the implementation of the RDR has been well-publicised. Consolidators, some of whom are backed by private equity firms, state that they frequently pay cash up front when acquiring an advisory business and that they are looking for quality in the target firm's client bank and in its advisers – though of course, they would say that wouldn't they?

Our discussions with consolidators have led us to the conclusion that transactional activity will continue as advisory firms continue to decide whether they wish to remain in the industry or not. Recent headlines, for example, that Towry are in discussion with 85 firms, confirms this ongoing activity. As with process-focused advisory businesses, consolidator firms have prepared in advance for RDR and can therefore focus on their acquisitive activity, subject to their ability to access further capital.

3.5 NETWORKS

Transaction activity involving networks has been historically low because of the issues related to the financial performance of their low margin operating models. Our interviewees generally felt that these problems could be exacerbated by the arrival of RDR. This is because networks could struggle to attract and retain members resulting in further pressure on income with lower levels of profitability. It seems likely to us that RDR could be an additional catalyst of distressed network sales, which would be a continuation of a recent trend in such activity, as recently highlighted by the acquisition of The Whitechurch Network by the On-line Partnership Group in 2012.

3.6 CONCLUSIONS

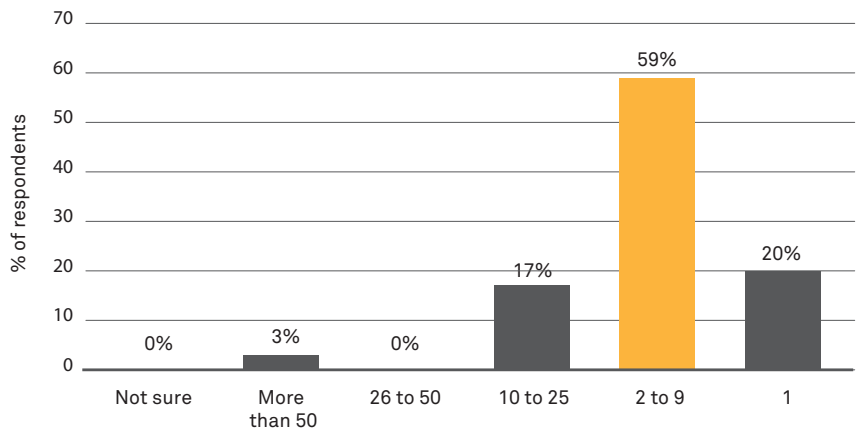
Our research suggests that RDR is likely to have had the greatest impact on smaller IFAs, who would not have had the necessary infrastructure to support RDR requirements, and may be more affected by the cash-flow limiting consequences of the elimination of trail income. The initial impact of the change is likely to be the creation of a greater number of advisory businesses ready to sell at discounted rates in distressed sales. The value of a book of business will be potentially much reduced with the abandonment of all trail income from 2016. However, because these sales are largely private, it is difficult to assess their impact at the lower end of the market. In relation to non-distressed sales, it is likely that it will take time for advisory businesses to build up a track record of transparent charging. In addition, the lack of a clear and widely agreed upon valuation metric in this initial period may have an impact on sales. Interviewees suggested that mergers and acquisitions activity may become subdued after an initial wave of distressed sales but will come to life in late 2014, once the new regulations are embedded and when advisers have a better understanding of what it will take to run a successful advisory business in this new regulatory environment. **However, the recent announcement by the FCA of the trail "sunset" clause will no doubt have an impact on this activity in coming months**.

APPENDIX: THE ON-LINE SURVEY

In order to review the RDR-related issues and concerns raised by our interviews with senior industry figures, we designed an online survey. The survey covered questions relating to the impact of the RDR on the adviser market, adviser business models and the valuation of advisory firms. It was sent to over 650 UK-based financial advisers; the results presented in this report are based on 64 responses received in March 2013.

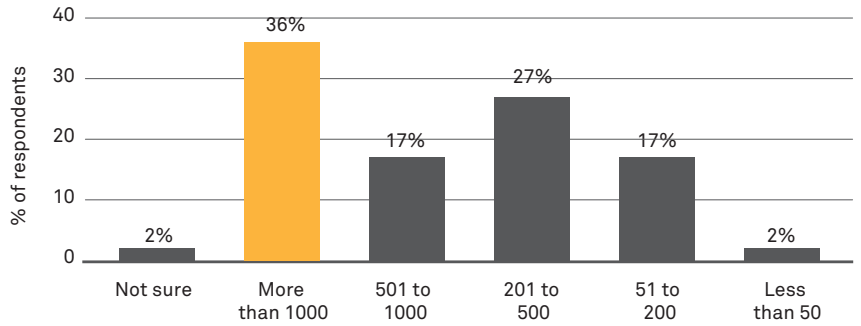
Figure A1 shows that 59% of respondents represented firms comprising 2 to 9 advisers; 20% of respondents were "sole traders"; 17% had 10 to 25 advisers; 3% of the respondents represented firms with over 50 advisers. We estimate the average number of advisers in our surveyed firms to be 8 advisers and therefore the majority of respondents can be considered to represent the smaller firm financial adviser community.

Figure A1: Size of firms represented in survey



The numbers of clients represented by the survey respondents is shown in Figure A2. 36% of respondents had more than 1,000 clients; 27% of respondents serviced 201 to 500 advisers; while the proportion of advisers that had 51 to 200 and 501 to 1,000 clients was 175 in both cases. We estimate that on average, there are 795 clients per respondent firm.

Figure A2: Number of clients



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