Jersey Financial Services Commission

FINDINGS OF MYSTERY SHOPPING RESEARCH

SUITABILITY OF ADVICE AND SALES PROCESS OF REGULATED INVESTMENT BUSINESSES

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1 Executive Summary

1.1 Introduction

The Commission has been responsible for the regulation and supervision of investment business undertaken in, or from within Jersey, since March 1999.

Though the Commission's routine supervision examinations formally capture documented information about sales processes, the Commission wanted to supplement these examinations with detailed insight into how the advice and sales process of regulated investment businesses is conducted in practice and viewed by consumers.

In recent years, the Commission has supplemented its themed examinations with two previous mystery shopping exercises. The first report was published in May 2008 and the second, based on a similar mystery shopping exercise, was published in February 2011 (the "**previous reports**"). The previous reports highlighted a number of key findings and identified various areas for improvement.

The Commission decided to repeat the mystery shopping exercise following the revision of the Codes of Practice for Investment Business (the "**Codes**") resulting from the introduction of the Review of Financial Advice ("**RFA**"). The Commission wished to see how the revised Codes were being applied in practice and whether lessons had been learned from the previous exercises.

Article 2(2)(c) of the Financial Services (Jersey) Law 1998 states that a person carries on investment business if the person gives investment advice, that is, the person gives to persons in their capacity as investors or potential investors advice on the merits of:

(i) the purchase, sale, subscription for or underwriting of a particular investment; or

(ii) the exercise of a right conferred by an investment to acquire, dispose of, underwrite or convert the investment.

The Attorney General granted authority under Article 35 of the Regulation of Investigatory Powers (Jersey) Law 2005 for the mystery shopping exercise to take place, which enabled the shoppers to record the meetings held without the knowledge of the advisers; transcripts of the recordings were used to assist with the analysis of the mystery shopping visits.

The Commission's objectives in undertaking the mystery shopping exercise were to obtain:

- Insight into the live dynamics of the advice and sales process of investment businesses; and
- Clear evidence, so that firms could be given clear and actionable feedback.

1.2 Methodology

This report is based on a programme of mystery shopping of scenarios all centred on a potential investment of a lump sum between £250,000 - £600,000. This is a similar scenario to one used in the previous reports. In none of the scenarios would the shoppers be considered to be professional investors; all were presented to the advisers as having little or no prior experience of investing of any kind.

A group of Deloitte staff and connected individuals conducted the fieldwork. The Commission provided a list of investment businesses, from which a sample was selected in order to carry out between twelve to fifteen mystery shopping reports; 14 reports were received. Each of the mystery shoppers contacted their assigned companies by telephone or in person to arrange an initial face-to-face meeting at the firm's offices to obtain advice on a potential lump sum investment.

Typically, the first appointment consisted of a discussion of the shopper's needs and normally included a fact find exercise by the adviser to establish the financial situation, attitude to risk and financial needs of the shopper. In eight of the mystery shops, this was followed by a second, and in two cases a third, meeting to receive advice and a recommendation on what financial products and services would meet those needs.

The mystery shopping interviews were conducted between 7 May and 31 July 2014 and have been undertaken using Mystery Shopping Providers Association Guidelines to benchmarking.

Whilst the mystery shoppers and the financial advisers were both male and female, for consistency, this report refers to them in the masculine form. Further details of the research methodology can be found in appendix A.

1.3 **Summary of key findings**

Findings resulted in relation to the behaviour of the adviser, the assessment of customer needs made, the advice received and the documentation and sales literature provided. Observations on best practice and areas for improvement are identified and summarised below.

The adviser

The behaviour of the advisers was considered in relation to how they introduced themselves and their firm, how they explained the services they offered and the charges for those services and whether the advisers sought to avoid any actual or perceived conflicts of interest through the advisory process.

Examples of best practice:

- Advisers provided terms of business and information about adviser charges and fees at the outset and supporting documentation for the shopper to read and digest at their leisure;
- Advisers informed shoppers verbally that they were regulated by the Commission; and
- Advisers explained the rationale for charges and the background to the recent move from commission to a fee structure.

Areas identified for improvement:

- Terms of business, fee information and other literature setting out the services provided were not provided at the outset and, where they were, the adviser played down the importance of these documents;
- A failure to set out for the shopper the context of the services being offered by the firm, with an implied assumption that the shopper was aware that the services offered by the adviser were of a particular type e.g. in-house investment management;
- Adviser remuneration came from commissions paid by the product provider, not from fees paid by the client as required by paragraph 4.8 of the Codes; and

- Where the adviser made use of product provider tools, no reference was made to that fact and, where that product provider was selected, the adviser did not make clear the potential conflict and set out the mitigating factors for the shopper.

The above failings could result in clients receiving advice and making investments without fully understanding the limitations, cost and terms of the advice provided, or the basis for such advice.

Assessment of customer needs

In all but two of the mystery shops, the adviser completed a fact find with the shopper or provided a questionnaire for the shopper to complete in his own time. The fact finding varied in depth and coverage.

Examples of best practice:

- A high level of information was sought, including personal details (individual and household), income and expenditure, any financial products held, level of 'emergency funds' required, details of loans (both secured and unsecured) and whether the shopper had a written will;
- An assessment of the shopper's attitude to risk with the use of a questionnaire or other risk assessment tool;
- Consideration of the risk appetite of both investors where a joint investment was proposed; and
- Advisers took the time to talk through the rationale behind the fact find and the risk assessment, to explain their relevance to an investor seeking advice on a lump sum.

Main areas for improvement:

- Even when the investor expresses a desire for advice on a lump sum only, sound financial planning guidelines should be offered to the investor to consider and included in the suitability letter issued;
- The investor should be given an opportunity to conclude independently on their risk appetite. A number of investors were led in this respect by the adviser suggesting a level which they felt was appropriate at the outset; and
- Financial objectives should not be assumed. In some cases advisers told investors that they should be looking for capital protection and income, rather than seeking to understand the shopper's individual situation and then offering detailed analysis of the types of investments that may be suitable.

Findings in the above areas could result in customers receiving an inadequate assessment of their financial needs and objectives and inappropriate advice for their current and long term financial circumstances.

Advice received

In all but four of the shopping scenarios the adviser focused only on the investment of the lump sum and did not make a recommendation that related to the overall financial needs of the shopper.

Examples of best practice:

- Product recommendations made were based on the shopper's risk profile, which included consideration of both the client's risk appetite and capacity for investment loss, his financial objectives and the period that he was prepared to restrict access to his money;

- The product, how it works and the associated fees and charges were explained in a clear and jargon free manner; and
- Recommendations addressed all key investment requirements, such as diversification across asset types and product providers.

Areas identified for improvement:

- Few advisers explicitly linked their product recommendations to the level of investment risk the client was willing and able to take, his financial objectives and, where applicable, the period that he was prepared to restrict access to this money;
- A failure to address any conflicts of interest apparent from the use of product providers' investment tools and recommendation of their products; and
- A failure to clearly set out all associated fees and charges as well as the key features of the service levels being provided.

Documentation / sales literature received

As identified in previous mystery shopping reports, documentation and sales literature is an area of weakness among most financial advisers that were mystery shopped.

The Codes require that "where a registered person is responsible for providing advice or exercising discretion for its clients, it must be able to demonstrate in writing that the advice or exercise of discretion is suitable for that client having regard to:

- The facts disclosed by that client;
- The terms of any agreement with that client; and
- Any other relevant facts about the client of which the registered person is, or reasonably should be, aware."

The Codes also require that "where a registered person is responsible for providing advice, it must make available to its client, in a comprehensive and timely manner, appropriate information so as to allow the client to make an informed investment decision."

Examples of best practice:

- Comprehensive and appropriate information about the products recommended is in the form of a 'suitability letter', from the financial adviser;
- Suitability letters include reference to:
    - an outline of the client's current financial position,
    - an outline of the client's attitude to risk,
    - an outline of the client's financial objectives, including liquidity requirements,
    - product recommendation(s),
    - information on the products,
    - information regarding associated risks, and
    - information on associated costs and fees;
- Advisers made use of product provider fact sheets, key investor information documents and platform information to supplement the recommendation information set out in the suitability letter.

Areas for improvement included:

- Advisers did not provide their clients with comprehensive suitability letters, which would result in them being unable to make informed investment decisions. Additionally clients were not given the opportunity to identify any areas where they might wish to seek further clarification or that had been mis-understood by their adviser;
- Advisers did not link a client's financial objectives to the key features of the products recommended; and
- Advisers provided too much information in the suitability letters, which was confusing for the client.

Other information

The professionalism of some advisers was questionable during the mystery shops, given the playing down of key documents and, in one case, a tendency to take an excessive amount of time in meetings with the client and then complain vehemently when the investor told the adviser that they would be investing their funds elsewhere.

2 Background

2.1 What is mystery shopping?

The Market Research Society defines mystery shopping or 'mystery customer research' as:

"The use of individuals trained to experience and measure any customer service process, by acting as potential customers and in some way reporting back on their experience in a detailed and objective way."

Mystery shopping is a long-established research technique and is used extensively in many industry sectors, such as retail and many large financial services providers, to measure the quality of service provided.

The Attorney General granted authority under Article 35 of the Regulation of Investigatory Powers (Jersey) Law 2005 for the mystery shopping exercise to take place, which enabled the shoppers to record the appointments without the knowledge of the advisers. Transcripts of the recordings were used to assist with the analysis of the mystery shopping visits.

2.2 Research Objectives

The aim of the Commission in conducting a series of themed on-site examinations is to concentrate on specific areas of conduct taken across a segment of the industry in order to obtain an indication of the standards and approaches being applied.

Though the Commission's routine supervision examinations formally capture documented information about sales processes, the Commission wanted to supplement these examinations with detailed insight into how the advice and sales process of regulated investment businesses is conducted in practice and viewed by consumers.

Consequently, in 2008 and 2011 and most recently in 2014, the Commission decided to supplement its themed examinations with a mystery shopping exercise and appointed Deloitte LLP to act on its behalf.

The on-site work conducted as part of this mystery shopping exercise has consisted of 14 separate mystery shops conducted by Deloitte LLP.

Specifically, the Commission's objectives in undertaking the mystery shopping exercise were to obtain:

- Insight into the live dynamics of the advice and sales process of investment businesses and retail banks; and
- Clear evidence for supervision purposes so that firms can be given clear and actionable feedback.
- As with all on-site examinations, a firm is assessed in terms of its compliance with the relevant Laws, Orders and Codes of Practice.

3 Key Findings

This section summarises the key findings from the mystery shopping exercise and covers findings relating to the adviser, assessment of customer needs, the advice received and the documentation/sales literature received. Some observations from the mystery shoppers are also included.

3.1 The Advisers

This section reviews the activities of the advisers under three main headings:

Introducing the firm - examines the extent to which advisers explained to the shopper the range of services that the firm provided, how the firm was regulated and whether they were restricted in the range of product providers that they could advise on;

Commission or fees - considers how clearly the adviser explained the manner by which they and the product provider were remunerated and whether this was in compliance with the Codes; and

Impartiality of advisers - notes whether advisers were suitably independent of the product provider to prevent any actual or perceived conflicts of interest.

3.1.1 Introducing the firm

The Codes state that a registered person "must disclose on its stationary and in advertising material that it is regulated by the Jersey Financial Services Commission".

All 14 investment business advisers supplied a business card, although only six provided a copy of their Terms of Business. All Terms of Business documents given to the mystery shoppers disclosed that the Commission regulated the firms.

One of the 14 firms provided product literature to shoppers on one of their investment businesses' own products and this contained the required disclosures.

Seven of the 14 advisers also verbally stated that their firm is regulated by the Commission.

11 of the 14 firms told the mystery shoppers something about their firm and the services offered, although the quality of description varied significantly from adviser to adviser. Three of the advisers provided the shopper with no details either about the firm or range of services offered. Where proposals were offered by advisers with an in house investment management team, no effort was made to draw out the difference in services offered to that of a conventional IFA. The proposals did, however, set out that they were offering a discretionary investment management service somewhere in the documentation.

In one instance, whilst the adviser provided Terms of Business, he played down the relevance and importance of the document.

> **"...these are the terms and conditions and this bit on the back is something that is optional and is part of the regulation and asks you various information about your life style so on and so forth and you can fill it out as much as you would like to at the end of the day. Some people find it quite intrusive!"**
>
> ***Retirement planning scenario***

3.1.2 Commission or fees

The Codes state that a registered person "is required to demonstrate in writing that the client has been made aware of all associated fees and charges including commissions (both initial and recurring), where these are permissible, and any payments to or from third parties (such as introductory fees or commission sharing arrangements)".

Clarity of the explanation of fee structures varied from adviser to adviser. In five of the 14 mystery shops the advisers clearly explained the structure of charges applied by both the firm and the product provider during the meetings. Two advisers failed to make reference to fee structures in the meeting or subsequent recommendation documents and the remaining advisers relied upon terms of business or suitability letters to provide such information to the client. Where advisers provided terms of business these set out clearly how fees and charges would be applied.

Best practice observed during the course of this exercise included the adviser explaining the background to the change in charging structures to set the scene for the shopper and help them understand the rationale for the fee charges in place. Overall, however, emphasis on fee charges and the clarity of the explanation should be enhanced to ensure that the investor has a sound understanding at the start of the meeting of the charges in place for advice and ongoing services.

> **"It doesn't really matter to us whether you're with one fund or with a hundred funds; we get paid the same because we are going to come to a fee agreement."**
>
> ***Retirement planning scenario***

Since the last mystery shopping exercise was undertaken the Codes have been revised by the Commission's Review of Financial Advice. The Codes now require financial advisers to adhere to the following;

"A *registered person* carrying on Class C or Class D investment business is not permitted to receive remuneration by way of commission from product providers for investment advice services provided to Jersey resident *Retail Clients"*

All 14 advisers held either a C or D investment business registration and, of those 14 advisers:

- two advisers charged fees for the initial consultation as well as ongoing advisory fees;
- nine advisers set out their fees payable upon investment and then annual advisory fees;
- two advisers charged only on-going advisory fees; and
- one adviser set out in their advisory terms of business that they will normally receive commission on the sale from the product provider. No reference was made to fees paid by the shopper to the adviser.

> **"If you buy a financial product. We will normally receive commission on the sale from the product provider. Although you pay nothing up front this does not mean our service is free. You still pay us indirectly through the product charges."**
>
> ***Retirement planning scenario***

3.1.3 Impartiality of advisers

Given that financial advisers must now be remunerated directly by the client and receive no commission from the product provider, it would be expected that the financial adviser would be free from any conflict of interest arising from methods of remuneration.

However, a number of advisers made reference to, and use of, tools provided by investment product providers which may reduce costs for their business and thereby, create an incentive to recommend the product providers services. In the example of one platform provider, four advisers used their risk assessment tool to generate a risk profile of the investor and two of those advisers went on to recommend products on their platform, one of whom ultimately recommended the platform providers own funds.

> **"…we've used Firm O to show you the risk analysis and how we break it all down in our model portfolios. It doesn't necessarily mean that we're going to put you into Firm O."**
>
> ***Lump sum scenario***

Other advisers went directly to investment managers that they were familiar with, without explaining what research they had done in relation to the selection of these managers.

No other potential conflicts were noted as a result of the mystery shopping exercise.

3.2 Assessment of customer needs

This section presents the results of the fact finds that were conducted. It explores:

Client Classification – the extent to which advisers identified the shoppers as *Retail Clients* or *Professional Clients* as defined by the Codes;

Assessment of financial situation - the completeness and the thoroughness of the assessments of the financial situation conducted;

Affordability - the extent to which advisers ascertained that the shoppers had some emergency cash available;

Attitude to risk - the time advisers spent explaining risk and in making sure that the shoppers understood the concept;

Financial objectives - considers whether the adviser assessed what the shoppers understood about the terms capital growth and income; and

Other matters - conduct of the advisers.

3.2.1 Client Classification

No reference was made by any of the advisers as to whether the mystery shoppers would be treated as a *Retail Client* or a *Professional Client*.

It is assumed in all cases that shoppers were treated as *Retail Clients* given that no reference was made in conversations with the shoppers, or suitability letters, as to the basis upon which they were to be treated.

3.2.2 Assessment of financial situation

The Codes state "where a registered person is responsible for providing advice to or exercising discretion for its clients, it must obtain, document and maintain any information about the circumstances (both financial and otherwise) and investment objectives of the client that are relevant to the services to be provided."

> **"Obviously the more information you give us the better…….if you don't want to answer it it's only on the investment sum that you've got."**
>
> ***Lump sum scenario***

All advisers took time to understand the background of the mystery shopper, where the money for investment had originated from and the investment goals of the investor.

The majority of advisers used a pro-forma questionnaire or equivalent. Consequently, there was consistency in the range of questions asked by each of the advisers during the meetings. Typically these included:

- Personal information (name, address, marital status, dependants, employment, annual personal and household income);
- The financial products held (pensions, savings and investments, mortgage, life assurance, other protection); and
- Health status (smoker/non-smoker, general fitness).

All shopping scenarios used related to the investment of a lump sum and the extent to which advisers looked beyond the lump sum investment, and the requirements given by the shopper for the funds in the future, varied.

Seven advisers did not ask the investor if they had any unsecured loans and only six of the advisers discussed requirements for other financial products beyond the investment of the lump sum described.

> **"one of our principles is that, if clients have got borrowing they should seriously think about paying that off before they take their longer term investments"**
>
> ***Lump sum scenario***

3.2.3 Affordability

Given the mystery shopping scenarios used, it would be expected that the adviser would consider the need to retain some of the funds being invested for future expenditure, especially where the investor was proposing to retire, as a number were.

It was therefore positive to see that the majority of the advisers (10 out of 14) enquired as to whether the shopper had emergency funds/'rainy day' money. Seven advisers set out an appropriate amount to be put to one side and explained the purpose of the amount.

Other advisers allowed the shopper to make his own judgement as to whether the money he had put aside was sufficient for his needs.

> **"The basic rule is three times your monthly expenditure. But on a sum of £300,000… on that sum I would say at least keep £50,000."**
>
> *Lump sum scenario*

3.2.4 Attitude to investment risk

The determination of the level of investment risk that a client is willing and able to take was generally addressed through the use of a risk questionnaire. A number of advisers made use of the risk assessment tools offered through investment platforms, whilst others discussed risk attitudes with the investor using a diagram or other document as an aid. As such, the detail with which risk assessments were undertaken varied greatly, but the risk reward concept was generally well explained in 12 out of 14 mystery shops performed. Where advisers did not explain the risk versus reward concept in person, a detailed explanation was given in the suitability letter or recommendation provided following the meeting.

Best practice was to link the client's investment profile, which included consideration of the client's risk appetite and capacity for investment loss, to the features of the recommended investment solution.

Of the 14 shops undertaken, 11 advisers formally assessed their client's attitude to risk, with the outcome ranging between low to medium risk appetite, as was appropriate for the scenarios presented. The table below shows the manner in which the advisers approached the risk assessment. Of the 14 shops undertaken, four used a platform provider's questionnaire, three used in house risk assessment questionnaires, one used a financial consultancy firm's questionnaire, three used risk charts as an evaluation tool, and three did not assess risk.

Registered Person	Method of Assessing Risk
Firm A	Risk questionnaire – no conclusion given in meeting. Proposal based on low/medium risk.
Firm B	Risk grading chart used as an aid. Low/Medium risk determined.
Firm C	No risk assessment undertaken. Low risk rating confirmed verbally with client.
Firm D	Used third party consultant's risk assessment tool.
Firm E	Used platform provider's risk assessment tool.
Firm F	Used platform provider's risk assessment tool.
Firm G	No risk assessment performed.

Registered Person	Method of Assessing Risk
Firm H	Used platform provider's risk assessment tool.
Firm I	Risk discussed extensively but client does not conclude on risk appetite, nor is it assessed.
Firm J	Proprietary risk questionnaire.
Firm K	Risk chart used to assist client conclude on risk appetite.
Firm L	Proprietary risk questionnaire.
Firm M	No risk assessment undertaken.
Firm N	Used platform provider's risk assessment tool.

Amongst the three advisers who did not adequately assess the risk profile of the investor the degree of consideration given to the topic varied greatly.

> **"… at some point in time I'd probably like to go through the risk questionnaire. "**
>
> *Retirement planning scenario*

In one instance, the adviser did not seek input from the investor as to his risk appetite but explained why the investor would sit in the moderate risk category and proceeded with providing recommendations on that basis.

In another case no risk assessment was performed at all and investment recommendations were made on the basis of the adviser's view of the client's risk appetite.

One adviser assumed that the client should adopt a low risk investment strategy and suggested as such without discussing the link between investment risk and expected returns. No attempt was made to explain the different risk categories that an investor could choose for their investment portfolio.

> **"And presumably in terms of your risk appetite it's going to be low risk"**
>
> *Lump sum scenario*

Many firms asked the investor to complete an investment risk questionnaire in conjunction with their partner, where relevant, to ensure that both investors' risk profile could be considered. A number of advisers set out a requirement to meet the investor's partner where investments were to be made in joint names.

> **"it might be better to work through these questions together, to give a more general overview of your risk profile because then if we're investing in joint names, I would like this to be completed in joint names as well"**
>
> *Lump sum scenario*

One adviser did make a number of assumptions about the investor's approach to risk which seemed to be based on little more than personal opinion as shown below.

> **Mr A, I believe your life experience and training have provided you with a unique prospective [sic] on how things actually are, thus you are no stranger to risk. On the other hand Mrs A, you have used your knowledge and training plus of course 'woman's intuition' to establish constants (knee bone connected to the thigh bone etc.) prior to committing."**
>
> *Retirement planning scenario*

There were some good examples of the advisers taking the time to clearly explain the risks and the benefits of a diversified portfolio. However, caution should be taken when describing investment risk, as no investment can be risk free. One risk questionnaire defined low risk as "means you are not prepared to take risks with your investment". Another adviser, Firm B, stated in a discussion with the shopper that "when we look at wealth with the concept of diversification we can almost relay all of the risk". On the other hand the same adviser successfully identified a number of different risk types and explained them to the shopper.

3.2.5 Financial objectives

The quality of assessment of the financial objectives of the investors varied significantly across the advisers under review. All advisers established that advice in relation to a lump sum investment was required, but not all questioned the investor to establish the best use for the lump sum given their current financial circumstances. The table below gives a summary of the approach taken to establishing financial objectives by each adviser:

	Investor Profile	**Future Funding Considerations**
Firm A	Retirement planning	Full income and expenditure analysis and established no likely changes to financial requirements in the future.
Firm B	Retirement planning	Full income and expenditure analysis and established no likely changes to financial requirements in the future.
Firm C	Lump sum investment	Identified amount to be invested and requirement for capital or income but nothing else.
Firm D	Lump sum investment	Information disclosure levels driven by client. Advice was only given on the lump sum investment.
Firm E	Retirement Planning	Full fact find on financial position and understanding of expenditure requirements.
Firm F	Retirement Planning	Full fact find on financial position and understanding of expenditure requirements.
Firm G	Retirement Planning	Limited fact find. Future requirements not covered in any detail.
Firm H	Lump sum investment	Full fact find ensuring sufficient disposable funds on a monthly basis.
Firm I	Retirement Planning	Full fact find and consideration of future income requirements and capital expenditure.
Firm J	Lump sum investment	Basic fact find and advice limited to lump sum advice at request of client.
Firm K	Lump sum investment	Advice limited to lump sum at request of investor but covered borrowing and rainy day fund requirement.
Firm L	Retirement Planning	Full fact find and consideration of future income requirements and capital expenditure.

	Investor Profile	Future Funding Considerations
Firm M	Retirement Planning	No fact find but established need for income and capital preservation.
Firm N	Lump sum investment	Full fact find and consideration of future requirements.

Only five advisers out of the 14 under review looked past the lump sum investment proposed to identify other areas for financial review. Products discussed included life assurance, income protection and pension provisions.

"If in the future you're looking at things like life cover or you extend your mortgage and you think, actually, I need to review that, we can provide quotes for you on those bases."

Lump sum scenario

Nine advisers discussed with the shoppers their plans for the future and how their financial priorities may need to change now, to allow their future plans to be achieved. However, these discussions generally centred on facts brought to their attention by the investor at the outset of the fact find and did not necessarily constitute a full review of their financial objectives.

"What I'll do, as I say, what this takes us through is your current situation, any assets that you have and liabilities, so that we can assess exactly where you stand financially."

Retirement planning scenario

3.2.6 Other matters

It is positive to note that no mystery shoppers were asked to conduct their investments on an 'execution only' basis, that is, no shopper was asked to sign a statement to say that he received no advice and that his investment decision and/or product selection was made of his own volition.

It was noted, when reviewing the transcripts and proposals offered to investors, that advisers were often happy to issue proposals before all facts had been established, and in some cases advisers were very reluctant to issue a formal suitability letter.

It is recognised that, due to timing restraints, some advisers were pushed by the investors to send proposal information, but caution should be taken by advisers where information in their possession was inadequate to offer meaningful recommendations.

The table below shows that the proportion of advisers who requested a second (or third) meeting with the shopper was over half of all mystery shops. The benefits of holding at least a second interview include allowing the adviser sufficient time to make a considered recommendation, allowing the adviser to explain the recommendation to the shopper and to give the shopper the opportunity to consider and to ask questions about the recommendation.

One meeting	Two meetings	Three meetings
4	8	2

3.3 Advice received

This section presents the findings relating to specific areas that were identified during the advice process and includes:

Financial needs identified - explores whether the advisers identified financial needs, other than to invest savings;

Rationale given for final recommendation - to identify if product recommendations are made with reference to the output from the fact find and if any recommendations are made that appear to be influenced by any other factors;

Clarity of product explanation - the clarity with which the products recommended are explained to the shopper and whether penalties had been discussed; and

Other information - presents other observations on the advice received as well as the advice process.

3.3.1 Financial needs identified

A review of the advice received shows that the majority of advisers focused primarily on the investment of the lump sum. Of the 11 suitability letters received, four considered financial needs beyond the lump sum investment discussed. Three of the advisers stated the advice was limited solely to the lump sum amount.

> **"After reviewing your client profile, risk tolerance questionnaires and taking into account your personal objectives I would recommend an International Investment Bond as a suitable investment vehicle."**
>
> ***Lump sum scenario***

The four advisers who considered financial needs beyond the lump sum, set out advice in their proposal documents which included:

- Recommending a will be put in place if necessary;
- Recommending that the shoppers seek tax advice;
- Private health insurance;
- Rainy day funds; and
- Life and Critical illness cover.

Where the shopper was considering moving to Jersey, the better advisers mentioned a variety of factors for consideration including Jersey social security and income tax considerations as well as, on a couple of occasions, housing license considerations.

> **"I mentioned the issue of UK inheritance tax and you have advised that advice has already been sought in the UK and you believe there to be no liability."**
>
> ***Retirement planning scenario***

A number of advisers presented recommendations without any reference to the limitations of their advice and offered lump sum investment advice with little context.

3.3.2 Rationale given for final product recommendations

Of the 11 advisers that produced formal proposal documents, all advisers stated the financial objectives of the shopper. In most cases they went on to make a recommendation but not all drew a link between the key features of the products and how they satisfied the objectives of the client.

Examples of where this link between objectives was clearly demonstrated to the shopper included:

- Determining the risk a client is willing and able to take and linking the specific risk factors of the proposed investments to them;
- Demonstrating the capital growth or income generated historically as a supporting factor for the selection of the fund going forwards, with the appropriate caveats relating to historic performance not being an indicator of future performance; and
- Explaining the concept of diversification across asset classes and how this might optimise returns for the level of risk embraced.

By contrast there were a number of examples of suitability letters that did not assist the reader to understand the rationale for the recommendation:

- Use of complex terminology without adequate explanation. This terminology had not been used in the identification of objectives or elsewhere in the document so it could not be expected that the shopper would have a clear understanding of the reason for the recommendation;
- A failure to link, in any way, the portfolio of assets recommended to the objectives set out in the covering letter; and
- Inclusion of so many benefits in relation to the product that is hard to identify if it actually addresses the requirements of the shopper.

> **"I have selected the funds shown below based on my assessment of the level of investment risk you wish to take and your specific investment objectives."**
>
> ***Lump sum scenario***

Advisers often made reference to a number of additional benefits provided by the products set out in the recommendations. Such benefits included flexibility, cost effectiveness, adequate diversification, tax efficiency and liquidity. All of these benefits were relevant to the shopper scenario presented.

A number of advisers failed to include sufficient information in suitability letters, or did not include important documents that would assist the client in their decision making. Examples included:

- Key features document not sent with proposal to support recommendations;
- Letter did not cover charges, penalties or cooling off period in sufficient detail;
- Letters did not cover alternative products considered in some cases; and
- Letters did not address details of investment switches.

3.3.3 Clarity of product explanations

Advisers frequently supported their recommendations with supplementary information including:

- Fund fact sheets;
- Personal illustrations;

- A personalised investment proposal from the manager selected, which included information on staff, investment strategies, investment approach and fees;
- Platform information; or
- Links to websites of the product providers.

Explanations were clearest where key features were drawn out in the suitability letter and the shopper was referred to additional information as required. This allowed the investor to link the key features of the product to their financial needs.

Where advisers provided substantial amounts of information concerning a number of different products, or where they made use of excessive technical language, it became difficult to extract key features and, thus, the basis for the recommendations.

> **"The smoother price after any adjustment will increase at the EGR for the quarter. The unsmoothed price is not published to avoid speculation over the possible smoother price adjustments and so protects the investors in these funds."**
>
> ***Lump sum scenario***

3.3.4 Other information

This section seeks to highlight any other issues that arose during the advice giving process.

One adviser, failed to link the timeline of the client to the investment proposed. In this case the client wished to invest funds for a period of five years before buying a house but the products recommended were identified as requiring a minimum investment timeline of 10 years.

In one instance an adviser, having made use of a platform provider's risk profiling system, then went on to recommend the platform but did not address the potential conflict arising in the recommendation given.

One adviser printed out the proposed portfolio showing line by line the assets which would be purchased but in no way linked this listing of assets back to the objectives of the client.

Such issues demonstrate a specific failure to adequately consider and document the appropriateness of the recommendation to the client.

3.4 Documentation/Sales literature received

This section reviews the level and appropriateness of the product literature received and includes:

Suitability letter - comments on the format and content of the letter and how quickly they were sent out to the shoppers or whether one appears to have been provided to the mystery shoppers; and

Other documentation - comments on whether other relevant documentation, such as, the key facts document and/or terms of business letter were received by the mystery shoppers.

3.4.1 Suitability letter

The Codes state that "where a registered person is responsible for providing advice or exercising discretion for its clients, it must be able to demonstrate in writing that the advice or exercise of discretion is suitable for that client having regard to:

- The facts disclosed by that client;
- The terms of any agreement with that client; and
- Any other relevant facts about the client of which the registered person is, or reasonably should be, aware."

The Codes also state that "where a registered person is responsible for providing advice it must make available to its client, in a comprehensive and timely manner, appropriate information so as to allow the client to make an informed investment decision."

The Commission issued a guidance noted in 2008 called 'Suitability of Advice', which outlines its expectations that suitability letters are issued prior to any transaction taking place. 11 out of the 14 firms, where the adviser made a recommendation, had sent suitability letters to the mystery shoppers. Three shoppers experienced difficulty in obtaining a recommendation in a timely manner. One adviser was awaiting investment committee approval to offer platform investments which would represent better value for the shopper, one adviser failed to offer a formal recommendation after meeting with the shopper three times and one adviser issued proposal documents direct from the investment manager and suggested that he would offer a formal recommendation once the shopper had decided which proposal to go with.

> **"The reports are quite detailed, I was therefore going to suggest a meeting to ascertain the most appropriate proposal prior to making a recommendation. If required meetings can be arranged with the fund managers to answer directly any questions you may have."**
>
> ***Retirement planning scenario***

The format and content of the letters received by the shoppers ranged from firm to firm, from comprehensive formally bound and structured reports to, in one instance, a short informal email outlining the recommendation. The more formal suitability letters included:

- an outline of the client's current financial position;
- an outline of the client's investment risk profile;
- an outline of the client's financial objectives, including liquidity requirements;
- product recommendation(s);
- information on the products, such as key facts documentation;
- information regarding associated risks; and
- information as to the associated costs and fees.

The clarity of the letters varied in terms of the linkage between the client's needs, investment risk profile and length of time they were willing to invest. As is detailed in section 3.3.2, some advisers did not adequately explain complex terminology so that the shopper could make an informed investment decision.

3.5 Other findings

This section covers specific comments made by some of the mystery shoppers on the difficulty experienced in arranging an appointment with a financial adviser.

3.5.1 Behaviour of Advisers

The majority of advisers were responsive, amenable and professional, but one shopper highlighted the response received from their adviser as lacking professionalism. Despite the shopper making clear to the adviser that they were considering proposals from a number of advisers, the below quote comes from an e-mail sent by the adviser upon being informed that the shopper would not be taking up the recommendations offered.

> **"I set aside other clients' needs and spent considerable time not only assessing your requirements but preparing a personalised report for your further consideration; this report although not fully complete due to time constraints was to be used today to discuss the finer details with you and Mr A, whom I was looking forward to meet [sic], and only then, if all was in order would I have finalise [sic] proceedings on your behalf. Alas, that did not happen and I now find myself out of pocket but a little wiser."**
>
> ***Retirement planning scenario***

The Principles of the Codes require that registered persons operate with high ethical standards. Registered persons must have the highest regard for the interests of their customers. In this instance the adviser demonstrated behaviour that fell below these standards.

3.5.2 Time Spent on Each Mystery Shop

The time spent by the shoppers in meetings with financial advisers varied significantly. In one instance a meeting lasted under one hour and in another in excess of two and half hours. Whilst it is recognised that developing a relationship with the client and spending the time to truly understand the clients' viewpoint, preferences and objectives is crucial, mystery shoppers did feel in some cases that meetings lasted too long. Transcripts indicate that the one adviser who held a meeting of two and a half hours with one shopper, had a tendency to cover the investment markets, investment options and economic issues to such depth that the shopper became confused by the information they were receiving. Consideration should be given to detail covered in the meetings, such that the adviser does not confuse and fatigue the shopper.

One adviser required three meetings with the shopper and still failed to produce a formal recommendation after three meetings had been held.

Appendix A - Research Methodology

The Commission provided Deloitte LLP with a list of 24 investment businesses that are registered to give investment advice ranging from small independent financial advisers to large retail banks.

The Commission also tasked Deloitte LLP with presenting the 'shopper' with a set of circumstances that we would expect would trigger a need for a particular product or service. This resulted in the selection of the lump sum scenario for research purposes. The Commission and Deloitte LLP together agreed 'ideal profiles' of the mystery shoppers for the scenario.

The profile of shoppers for the lump sum scenario required that individuals should have:

- An average income or retirement income;
- Some savings and investments;
- Dependants; and
- Some existing financial products, e.g. life assurance, pension, critical illness covers, mortgage protection, etc.

A group of Deloitte staff and connected individuals conducted the mystery shopping fieldwork. In each of the mystery shop scenarios, the shoppers used their real personal details at all times as well as their real financial details.

The mystery shop visits

Deloitte selected 16 investment businesses and allocated to each business a mystery shopper with a lump sum scenario. From these, 14 usable mystery shopping reports were received. One mystery shopper had to abandon discussions with an adviser after concerns were raised by the shopper about using the financial adviser in the future and one mystery shop was disregarded as the voice recording device did not record the first interview undertaken.

Each of the mystery shoppers contacted their assigned companies by telephone to arrange an initial face-to-face meeting at the firm's offices, seeking advice on what to do with their potential lump sum investment.

Typically the first appointment consisted of a discussion of the shopper's financial situation and included a fact find exercise to establish the financial situation of the shopper, his attitude to risk and to identify his financial needs. In eight of the mystery shops, this was followed by a second, and in two cases a third, meeting to receive advice and a recommendation on what financial products and services would meet those needs. Where only one visit was undertaken, the adviser provided his recommendations, either at the meeting, by post or by email. Three advisers failed to provide a formal Suitability Letter, although the shopper was provided with a discretionary investment proposal from another third party firm.

The mystery shoppers completed a detailed questionnaire based on their experiences of the appointment and the adviser. Each of the appointments was recorded by the shopper without the knowledge of the adviser. Transcripts of the recordings were used to assist with the analysis of the mystery shops, which were assessed under the following categories:

- The adviser;
- Assessment of customer needs;

- Advice received; and
- Documentation/sales literature.

The mystery shopping appointments were conducted between 7 May and 31 July 2014.

Research limitations

The project was required to complete a minimum of 12-15 mystery shops from a population of 24 firms provided by the Commission. In a small island like Jersey, the pool of mystery shoppers from which to recruit suitable assessors is limited. In the event, 14 usable mystery shops were completed. This relatively small number of mystery shop interviews makes this a qualitative research project. As such, the findings are not statistically reliable but, where appropriate, the number of instances where an observation is made is noted. The appointments were held with only one or two financial advisers from each business and therefore may not be indicative of the general standard of a firm's sales process. The findings provide an overview of the sales process adopted by individual advisers within the firms visited.