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THE ANATOMY OF **A CENTRALISED INVESTMENT PROPOSITION**

The regulator's perspective

FG12/16 Assessing suitability: Replacement Business and Centralised Investment Proposition contains two themes in one. The paper explores the effect of switches and the construction of a Centralised Investment Proposition (CIP). Great emphasis was placed on ensuring that any recommendation was in the best interest of the client, both in the advice stage and in checking suitability when constructing a portfolio. It is clear the FSA wished to ensure that the investments match the client's attitude to risk and that still is the case. It's an in-depth guide and provides clear pointers regarding how the regulator would like to see investment solutions constructed.

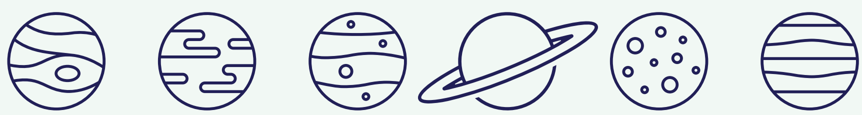
The fundamentals of a CIP

Fundamentally a CIP is a way to make sure you look at all the investment solutions out there, and after fully understanding your client's goals, create the best solution. The trick is to assemble all the moving parts into a logical methodology that works, is flexible and future proof.

There are two key areas to consider, from which everything will cascade, they are your client bank and all the Relevant Financial Instruments (RFIs) you can use with your clients, and it's a very broad brush, from cash and deposit funds at one end of the spectrum, through to risk managed solutions, bonds, IHT solutions up to and including platforms and products.

CLIENT BANK

INVESTMENT, PLATFORM & PRODUCT UNIVERSE



From this starting point, segment your clients and sort out which RFIs you will include and exclude from your CIP. Remember the Regulator does not prescribe what a CIP should look like but it does need to be logical and justifiable.

With regards to the client bank, the segmentation should be outward facing, not inward. What we mean by that is, the segments should be based on particular client circumstances and/or needs such as pre and post retirement. Do not segment based on the client's worth to you as a business.

In addition, when assessing RFIs, it's not enough just to say that certain solutions will be included or excluded, there should be a justified reason as to why.

Segment clients

Based on circumstances

Financial instruments

Included in the CIP

(with justification)

Financial instruments

Excluded in the CIP

(with justification)

The anatomy of a CIP

Consider exactly how a CIP is built, what are the moving part and how do they fit together.

A CIP should be a **DETAILED METHODOLOGY** on how you arrive at the most appropriate investment and tax wrapper solution for identified client segments, taking into consideration REGULATOR EXPECTATIONS.

As it is a methodology, it should not contain references to any particular investment product, platform or investment solution, the CIP is an instruction manual on how you filter the market to find the most appropriate course of action for your clients, or segment of clients.

When you **EXECUTE A CIP**, using research software, a shortlist of products, platforms and investments will be created.

If you are creating a CIP you should consider the following:

1. Describe who has responsibility and manages the CIP.
2. Incorporate **PROD** so you can;
   a. **SEGMENT CLIENTS**.
   b. Assess all the **RELEVANT FINANCIAL INSTRUMENTS (RFI)** in the marketplace and state which will be included or excluded along with justification.
   c. Make sure the right RFIs are used for the right clients.
   d. Ensure there is **NO SHOEHORNING**.
3. **RESEARCH AND PERFORM DUE DILIGENCE ON ALL THE RFIs** you include in your CIP, **WITHOUT RETROFITTING**.
4. **RESEARCH AND PERFORM DUE DILIGENCE ON PRODUCTS AND PLATFORMS, WITHOUT RETROFITTING**.
5. Describe how you will **MONITOR THE CIP** to ensure it remains fit for purpose.
6. Detailed Methodology: When I say detailed, I mean detailed. To the point of stating the obvious, think of the easiest question you could be asked and your CIP should cover it off.

So let's look at each of the areas highlighted previously.

Detailed Methodology

A Firm should be looking to describe the exact steps they go through when deciding the most suitable solution for a client, imagine an alien came down to earth and asked you how to make a cup of tea. How would you describe it? It's not sufficient to just say "Put the kettle on" because an alien doesn't know what a kettle is, or how to "Put it on". The same thing applies to a CIP, explain exactly how you do everything, and assume your audience has zero financial services experience.

The methodology then becomes logical, robust and forms the chapters within your CIP. Below are the areas to consider, and we'll expand upon them throughout this document.

Regulator Guidance

Understand and action the guidance from FCA Factsheets, Finalised Guidance, Thematic Reviews and any other relevant publications. The most perfect starting point is to first understand what the Regulator sees as important and what they expect from a CIP. Consider extracting the relevant parts of FG11/5, FG12/16, TR14/21, TR16/1, Factsheets 011 and 012 and MiFID II. All these documents contain direction on how to create a CIP.

Governance Framework

Identify those who will manage the Investment Proposition and define their roles. It's important to explain who has the responsibility to create, monitor and maintain the CIP. We work in a fast paced industry and legislation continually evolves, so should the CIP and therefore it should also evolve.

Platform, Product and Investment Philosophy

Identify the important aspects in selecting products, platforms and investments. This is the life and soul of a CIP and will make it unique to a Firm. The framework put together here is just that, a framework with no substance. This is where a Firm will start to form how it invests, what it invests in and what it believes are the most important aspects when creating good solid client outcomes.

Product Governance

Outline procedures to identify client segments and the relevant financial instruments. Not so much the strict PROD definition from the Handbook, but more so looking at the PROD method of segmenting clients and assessing those financial instruments available. This is the engine of a CIP. It orders the investments, platforms and products a Firm will consider and it enables the CIP to flex, so it can adapt to the changing demands of the financial services industry.

Platform, Product and Investment Selection

Create a process to undertake research and due diligence, identify investment, platform and product solutions suitable for an individual client or a segment of clients. So you've identified each of the RFIs you will have within your CIP. Now is the time to consider which, in each RFI, is the best. If a Firm states that they will use risk controlled multi-manager funds for instance, document exactly how they will conduct research and due diligence to arrive at a shortlist of the best of breed.

Method of Delivery

Document what will be provided and how it will be provided. The Regulator expects the advice process to be clear, fair and not misleading and this becomes the benchmark for creating a CIP. TR14/21 goes into great detail on what is expected so it's important to make a statement to this effect in a CIP.

Review Procedure

Have review and version numbers on documents, diarise the review date and maintain a change log. Here a Firm should look to manage their CIP and it's methodology to make sure it's still fit for purpose. The Regulator identified that Firms with good controls in place demonstrated a culture of challenge, so that they continually looked to refine areas within the business, such as the CIP.

REGULATOR EXPECTATIONS

How do you know if you're doing it right? The people who matter are the ones that can tell you if they think you're doing it right. That would be the Regulator.

You can see the Regulator as a hindrance or you can see them as guidance, what you can't do is ignore them. There's some great stuff out there which will tell you what the Regulator would expect to see in a CIP and the granddaddy of all the publications, is the mighty FG12/16, that's the one about what a CIP should look like.

Once you have a good idea what the Regulator expects you to do then put that in your CIP and next to it put down how you are going to do what the Regulator expects you to do. When I say detailed, I mean detailed. To the point of stating the obvious.

PROD

Product Governance in it's simple form is making sure you use the most appropriate product for your clients, it's common sense and firms do it every day. Make PROD the driver of a CIP and it works beautifully. It's made up of two main elements, (1) segmenting your clients and (2) identifying, then using Relevant Financial Instruments.

SEGMENT CLIENTS

The classic gold/silver/bronze client segmentation all came about because up to and during the introduction of RDR providers said, "Firms should segment their clients" and firms said "What's the best way of segmenting clients" and providers said "Segment them Gold/Silver/Bronze, based on assets under management". And so an urban myth was born.

From a PROD perspective, segmentation should be based on client needs, commonalities seen within a client bank and certainly not on how much worth they are to a business. In practice, when we do this exercise with IFAs during our consultancy work they struggle with the concept, but after talking it through it's usually the major lifetime event which sets segments, that being pre / post retirement.

RELEVANT FINANCIAL INSTRUMENTS

Toolbox analogy coming up. Your CIP is a toolbox, you fill it with the tools to enable you to do a job based on what that job requires.

Your CIP (toolbox) should look at all the financial instruments out there and you decide whether they are included or excluded. Then you decide which is the best financial instrument (tool) to satisfy client needs (the job) .

Not only should you decide, but add detailed justification. When I say detailed, I mean detailed. To the point of stating the obvious.

SHOEHORNING

Don't do it. If a client doesn't quite fit into a segment (which leads to certain financial instruments), then don't force them. Have a segment entitled "Bespoke" where you will advise from the whole of the market and consider every financial instrument out there.

INVESTMENT RESEARCH AND DUE DILIGENCE

Obvious one this, when you have identified the financial instruments you are going to use, have a logical credible process to filter down the market to the best of breed, based on your own filtering process. Then conduct additional due diligence if required.

PLATFORM RESEARCH AND DUE DILIGENCE

This isn't a typo, I repeat myself: Obvious one this, when you have identified the financial instruments you are going to use, have a logical credible process to filter down the market to the best of breed, based on your own filtering process. Then conduct additional due diligence if required.

RETROFITTING

Don't do it. It's not about the adviser, it's about what's the best fit for the client / segment of clients. PROD deals with this, for each relevant instrument have a detailed, client led, credible filtering process which enables you to logically select the best. When I say detailed, I mean detailed. To the point of stating the obvious.

From experience, in a lot of cases a firm will select down to the financial instrument they are currently using, this happens with Platform selection quite often, with investments not so. Usually there are a few good surprises unearthed.

EXECUTE THE CIP

If you are creating a CIP and you're doing it to satisfy the Regulator, then you don't use it in your advice process, then don't do it. The best thing you can do, as this is now obviously exactly how you would create a strategy, is to follow it.

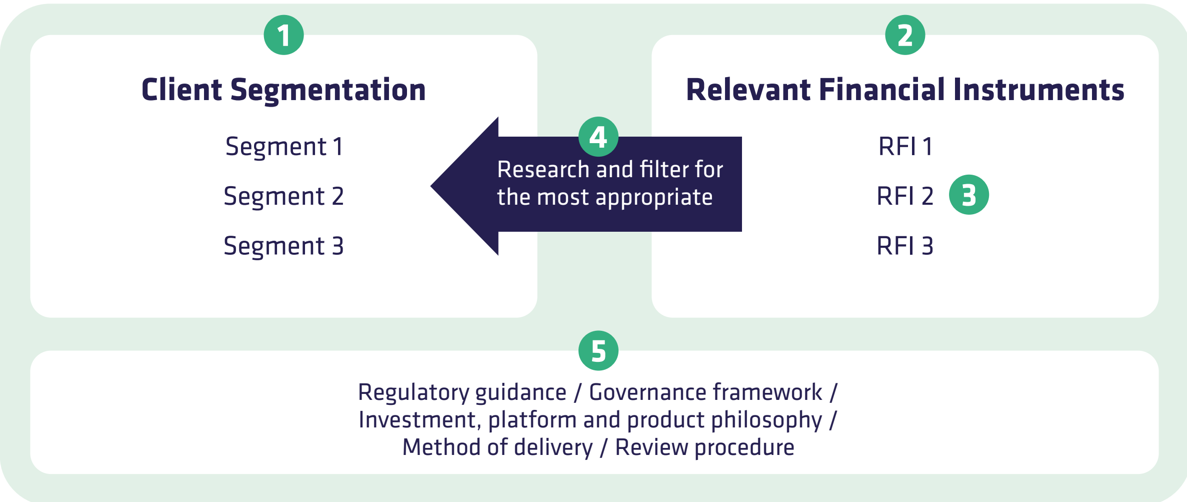
Make your process faster by taking the filtering process and mechanising it as much as possible by building filters into your research software. This is the bit where you get stuff out of your head and fully documented into a CIP and then into research software to make it happen in the real world.

As it is a methodology, there should not be references to any particular investment product, platform or investment solution, the CIP is an 'instruction manual' on how you filter the market to find the most appropriate course of action for your clients, or segment of clients.

MONITORING THE CIP

Consider RDR, the resurgence of PROD, MiFID II, retirement strategies, ESGs. Your CIP needs to flex, it should not stand still so there should always be a review of your CIP to make sure it's still fit for purpose, you're making sure that it's up to date, and demonstrating a culture of challenge within your business.

CENTRAL INVESTMENT PROPOSITION



1. Segment clients using common circumstances, ensuring a bespoke option
2. Identify the relevant financial instruments (RFI) to be used in the CIP
3. Use a filtering process on each of the RFIs to shortlist them
4. Identify the most appropriate RFIs to be used with each client segment
5. Take regulator expectation into consideration, manage the CIP through governance and the use of software tools

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