GUIDE TO PLATFORMS

● Execution only
3,425 advisers are scheduled to begin offering execution-only services to clients in the next two years. But how does this fit into advisers' current business models?

● Investment trusts
With 8,400 IFAs yet to adopt a platform, investment trusts could benefit from the number of advisers who look beyond platforms for investments

● Regulation
What, if anything, can experimental economics tell us about life after December 31 2012? Daniele Nosenzo, a professor at the Nottingham School of Economics, tells all

"The RDR has not been universally welcomed"

Daniele Nosenzo
Professor at the Nottingham School of Economics

"Regulatory change is bringing in new charging models"

David Barron
Head of investment trusts at JPMorgan Asset Management

"Platforms are ahead of the curve in charging their customers directly on a monthly or annual basis"

Linda Woodall
Head of investment intermediaries at the FSA

Left to right:
Linda Woodall, David Barron and Daniele Nosenzo

Execution-only could cause groupthink

The importance of high-quality advice – as opposed to a DIY or execution-only approach – lies at the core of the RDR. This concern is especially significant in the Google age, when so much in the way of supposedly wise counsel – to use the phrase very loosely – is so readily available and when quality, as a result, is vastly outweighed by sheer quantity.

There is understandable comfort in conformity. If we see others act in a certain way then we tend to emulate them – even if, as often proves the case, their conduct is mistaken, imprudent or downright nonsensical. In the age of mass information, these herd instincts can be amplified all too easily.

A number of studies have sought to confirm or deny the adage that "two heads are better than one", with most of the evidence that has emerged to support the claim coming from experiments that have compared group decisions with individual decisions. It could be argued that in reality many significant choices are better construed as individual decisions that involve an element of consultation.

For example, we might talk to family and friends before deciding how to deal with a health problem. We might solicit all manner of non-specialist opinions before buying a car. Or we might get some advice before choosing how to invest.

It is in these situations that consultation may cause difficulties, as they offer a tougher test of how those with the correct knowledge can convey it to others. To investigate this hypothesis, volunteers in Nottingham School of Economics' Centre for Decision Research and Experimental Economics (CeDEx) study were shown images of two paintings and asked to state which was by Paul Klee and which was by Wassily Kandinsky. Some subjects were placed in teams of six and invited to discuss the matter for five minutes, while others were asked to make their decision without conferring.

Individual decisions were submitted privately in both cases, with volunteers earning a cash payment for a correct answer and nothing for an incorrect answer. In the individual setting, 38 per cent answered both questions correctly, 33 per cent answered one question correctly and 29 per cent got both answers wrong. A similar proportion got both questions right in the consultation setting – 36 per cent – but 51 per cent got both wrong, while 13 per cent submitted only one correct answer.

In short, those who took part in group discussions were far less successful overall. Why? Well, because there was a tendency of teammates to give the same answers. In more than 80 per cent of teams a majority of the members gave identical answers to the two questions, and in about a third all six members concurred.

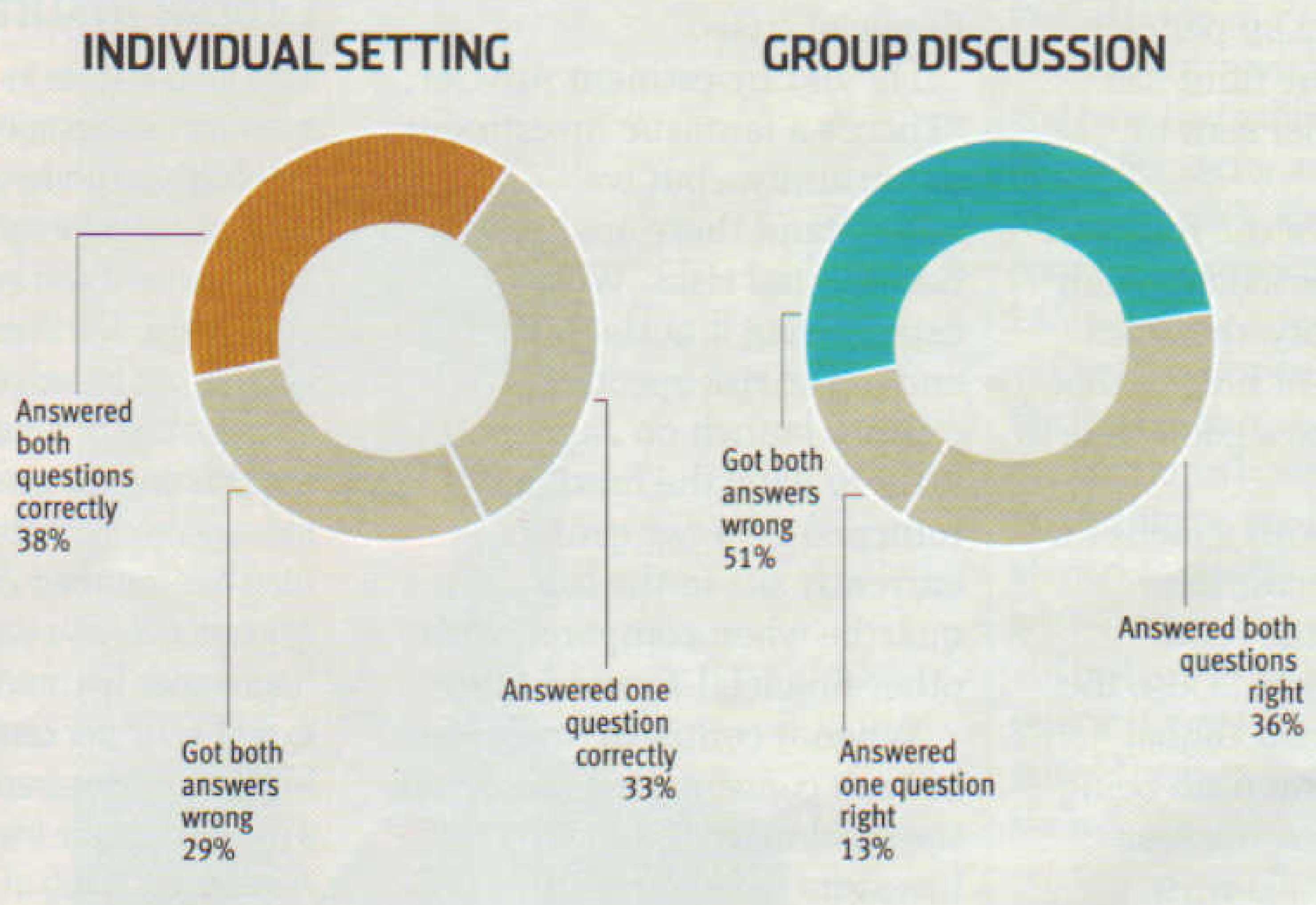
This happened even though participants submitted their answers individually, in private and having received no instructions that a team should reach consensus. Moreover, a post-experiment questionnaire revealed team members who reached a consensus believed communicating with others was helpful.

So it seems agreement makes us feel better but perform worse – or, to put it another way, individuals who know a little are likely to listen to a crowd that knows even less. We follow the herd – and the herd, unfortunately, is seldom well informed.

It is not necessary to be an economist, experimental or otherwise, to recognise the RDR has not been universally welcomed. The criticisms have been well documented. But even the concept's most strident detractors must concede it will deserve a measure of praise if it ultimately helps ensure truly worthwhile advice is heard and valued above the uninformed din – not least when a place among the misled DIY herd is otherwise so easily earned.

Dr Daniele Nosenzo is co-author of Does Consultation Improve Decision-Making, a study by the Nottingham School of Economics' Centre for Decision Research and Experimental Economics (CeDEx)

GROUP DISCUSSIONS ARE LESS SUCCESSFUL OVERALL



Source: Nottingham School of Economics' Centre for Decision Research and Experimental Economics

"'Don't get caught out.' This is sound advice for all as we prepare for the RDR"

The end of this year will bring the biggest change to the retail investment advice market in decades. Most advisers are well on their way to being ready.

Looking beyond the retail advice market, we have seen more providers launching clean share classes for their products, stripping out commission paid to the adviser – as well as the charge for the platform – on which the product is accessed.

These RDR compliant share classes of roughly 0.75 per cent, instead of the bundled annual management charge of 1.5 per cent, offer good value to clients and allow advisers to deliver a cost-effective solution that maximises the client's ultimate return on investment.

"The relevant market is defined by the client, not by the adviser"
Linda Woodall

As the RDR nears, many advisers have probably already decided whether their offerings will be independent or restricted from 2013. Some have asked how they can provide independent advice through a team approach.

Ultimately that personal recommendation must meet the standard of independent advice. It is the firm's responsibility to have appropriate systems in place to ensure each recommendation meets the required standard for platforms as well as the products they house.

Those who have considered going down the independent route have asked what is meant by the relevant market on which IFAs must offer advice. The relevant market is defined by the client, not by the adviser: it is whichever set of products is right for that client. So if, for example, the client only wanted to invest ethically, many investment solutions would be struck off the list. Global equities funds that have stocks in the oil and gas, tobacco and alcohol sectors would be excluded.

With the implementation deadline less than five months away, it's time to embrace the changes that both regulators and industry have worked so hard to achieve.

The onus is on the adviser to consider whether they should divide their clients into different segments with different needs, whether some clients will need an ongoing or a purely transactional service, how much the clients will be willing to pay and how they will pay.

Think about this now before it's too late. Any London-based advisers will be familiar with mayor Boris Johnson's catch-phrase for travelling during the Olympics: 'Don't get caught out.' This is sound advice for all as we prepare for the RDR.

Linda Woodall is head of investment intermediaries at the FSA