

JANUARY 2017

THE Review

CISI.ORG/REVIEW

PROVIDING INSIGHT AND ANALYSIS FOR FINANCIAL SERVICES PROFESSIONALS

Key events for 2017
How will Trump, Brexit and new regulation impact you?

The generation game
Does age affect approach to the financial planning profession?

Impact investing
Making a difference and a profit

**MOOLA CEO
GEMMA GODFREY
DISCUSSES MAKING
FINANCE SIMPLE**

**HOW ONE
INVESTMENT
MANAGER
HEADLINES
FESTIVALS**

Changing firms

WHO OWNS THE RELATIONSHIP
WHEN ADVISERS LEAVE?

OLD JOB

NEW JOB

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A LOOK INSIDE

Happy New Year to all our members! There are many changes affecting the financial services sector in 2017: Trump in the White House; Article 50; the Senior Managers and Certification Regime; elections in Hong Kong, France and Germany – turn to page 16 for a snapshot of key events to look out for.

Our academic supplement, the *Review of Financial Markets*, highlights growing interest in sustainable investing for 2017, and includes a detailed analysis (pp.41–49).

And for those who have resolved to change jobs in the new year, you may be asking yourself who owns the client relationship. Our ‘Changing places’ feature (pp.18–21) discusses this question from three points of view: an adviser, an employer and a client.

Enjoy the issue and the many other features not highlighted in these few paragraphs, and please do get in touch with any comments or suggestions.

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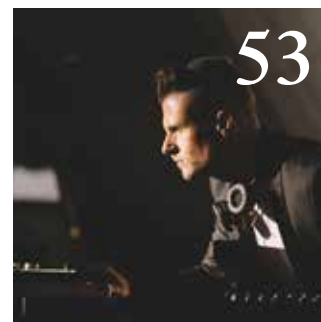
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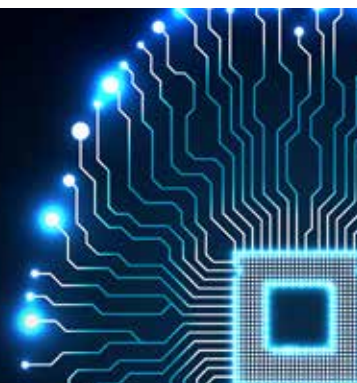
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The eight key principles for professionals

Your code of conduct is enclosed within this edition of *The Review*.

Read more on page eight
cisi.org/codeofconduct





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LIKE A THIEF IN THE NIGHT - THE £35BN STING

By stealth, the world's tax collectors have gathered together behind the backs of tax cheats and their advisers, and are all set to cosh them good and hard. By 2018, under the Common Reporting Standard (CRS) – covered in detail in our continuing professional development (CPD) article on pages 60–61 – more than 100 countries will be exchanging detailed tax information with each other, automatically.

In Britain, the process started in September 2016, with the first batch of data received by HMRC from the Crown Dependencies and British Overseas Territories – including the Channel Islands, Isle of Man and the British Virgin Islands. In a year, 54 further countries will be covered, and 47 more by 2018.

Britain's tax gatherers, under pressure from politicians and the public to help plug the uncollected 'tax gap' – currently reckoned at around £35bn a year, which is about half the amount contributed in tax by the financial services industry – have developed a powerful system, 'Connect', using software just a little below the standards used by the intelligence community. It now holds more data than the British Library, culled from banks, auction houses, salary details, social media, the lot.

In parallel, in many countries, the laws are changing and tax offences carry much more severe penalties, both for the evaders and for their advisers. From April 2017 in Britain, for instance, merely holding undeclared offshore income and gains will be a criminal offence.

Firms must now be more wary than ever of who they take – and keep – as clients. The authors of our CPD article, who have recently completed a lecture tour on CRS across the financial centres of the Persian Gulf countries and beyond, have commented

that "a number of firms are already seeking to de-risk their business models". In plain talk, that means dumping the dodgy clients. This may start a race to the bottom as evaders seek out similarly-minded, flexible friends in the financial community; but the tax collectors will welcome that concentration of targets in the Crocodile Islands archipelago.

Is this new tax campaign ethical and proportionate?

The technology being deployed by tax authorities is not the only parallel with the security and intelligence services. Lawful spying, in most developed countries, is governed by ethics and 'rules' in the same way that a just war is. That includes tapping phone lines and bugging bedrooms.

So is this new tax campaign ethical and proportionate? Every minute, yet more information is stored on all of us in 'the cloud'. Spying on that data – and other communications – in a legal, controlled and monitored manner is widely accepted as necessary if the lives of innocent citizens, under threat from terrorists and suchlike, are at risk. But does gathering data to increase the national tax takings tick the same box?

When General Michael Hayden was director of the National Security Agency – America's snooping agency, cousin to Britain's Government Communications Headquarters – he mapped out what his people did as a Venn diagram with three circles: legal, operationally relevant and technologically feasible. Later, as head of the Central Intelligence Agency, he added a fourth: politically sustainable. The new tax

disclosures seem to tick all these circles, not least as a populist storm sweeps the world.

The advent of a new Investigatory Powers Bill in Britain has brought renewed interest in, and concern about, how technology is being brought to bear on securing the state and its finances. David Anderson QC, in his independent review of the bill, suggests five principles for the use of such powers by the authorities: the law must be accessible and must work in a foreseeable way; the information gathering must be necessary, meaning more than just useful; the steps taken must be proportionate; there should be effective monitoring and oversight; and anyone mistreated must be able to get redress from an independent tribunal.

Again, the tax authorities' new joined-up powers seem, at least in the developed world, to tick the right boxes. But is this data gathering necessary, rather than useful?

On the evening of 11 September 2001, that line moved sharply in the intelligence world, substantially widening the target for 'necessary' surveillance. Growing disquiet about the evasion and avoidance of tax – and the blurring of the line between those two – has emboldened political leaders to take this tougher line with the errant. That estimated £35bn tax gap is a third of the budget for the National Health Service in England; this is not a trivial amount.

In the US, some 1.5 million people have 'top secret' clearance, including the likely next Edward Snowden, and the flood of information running between tax authorities will not remain secret for long. Firms must rapidly reconsider their risk profiles, and the nature of their clients, before they face potential reputational ruin.

60-SECOND INTERVIEW

The CISI and the Chartered Banker Institute have jointly launched a Certificate of Professionalism as third party verification to support the PRA/FCA Senior Managers and Certification Regime (SMCR). CISI Head of Membership Policy and CPD Audit, Colleen Peterson, Chartered FCSI, explains its value



Colleen Peterson,
Chartered FCSI

Why was it developed?

The SMCR, introduced in March 2016, requires firms to ensure the fitness and propriety of their staff.

The Certificate, when combined with evidence from the firm that employees are fit and proper for their role, will support this requirement by serving as third party verification to the PRA/FCA that employees have maintained their professional expertise and competence while upholding the highest standards of professional ethics.

It is a supplement to internal training requirements, not a substitute.

Who is it for?

Members of the two institutes can apply for the Certificate, which will be awarded provided they meet the required standards of professional knowledge and skills, continuing professional development

(CPD) and commitment to the relevant institute's code of conduct.

Those impacted by the SMCR are currently holders of senior management functions and employees impacted by the Certification Regime, but this will affect a wider audience in 2018.

What are the criteria?

The three components of professionalism – knowledge, skills and behaviour – must be demonstrated.

For the knowledge component, you need to hold at least a level 3 qualification recognised by the CISI, or a level 3 CISI qualification such as the Investment Operations Certificate, Investment Advice Diploma or Capital Markets Programme.

You can also apply via a 'Certificate by experience' route if you're a professional with a minimum of 15 years' work experience, who can demonstrate seniority, experience and relevant qualifications.

The skills component requires that you complete 35 hours of CPD relevant to your job role within a 12-month period.

Applicants must complete a CPD self-assessment form verified by their employer. The behaviour component can be demonstrated by signing up and adhering to the CISI Code of Conduct, passing IntegrityMatters (the CISI's online integrity test), and by completing five hours of structured CPD annually, on the topics of ethics, integrity, risk and regulation.

The Certificate is valid for a year, after which members will need to reaffirm that they have met the CPD requirements and upheld the CISI's Code of Conduct.

Certificate holders can apply for renewal two months before the expiry date, and the Certificate will then follow on from the expiry date of the current one. The CISI is working to provide an online renewal application form.

To apply

- Get in touch using the contact details in the advert opposite
- The CISI has updated its Code of Conduct. Visit cisi.org/codeofconduct for details

CHALLENGER vs ESTABLISHED BANKS

Who can restore trust in banking?

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19 January 2017 ★ 6 pm ★ Register for the webcast at cisi.org/integritywebcast

Certificate of Professionalism

We have worked with the Chartered Bankers Institute to introduce a Certificate of Professionalism for practitioners who wish to formally demonstrate an annual commitment to maintain their knowledge and skills and uphold the highest standards of behaviour.

The Certificate, combined with evidence from your firm, demonstrates to the FCA/PRA that you have met the requirements of the Senior Management and Certification Responsibility (SMCR) regime.

We will publish a public register of all our members who are successful in gaining this Certificate.

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The Review's quick quiz features questions from CISI *Professional Refresher*, an online learning tool. This popular product consists of more than 90 modules covering topics including anti-money laundering, the UK Bribery Act, information security and data protection. The answers are on page 15.

1. For how long can losses be carried forward to set against gains for capital gains tax purposes??

- A Indefinitely
- B One year
- C Three years
- D Five years

2. What was the principal purpose of the Financial Advice Market Review?

- A To consult on new legislation to prohibit commission payments for robo-advice
- B To discourage the development of online automated models for portfolio management
- C To encourage the development of affordable and accessible financial advice
- D To review the way in which MiFID was implemented in the UK

3. What is meant by the term 'advice gap'?

- A The difference in regulatory obligations between 'advisory' and 'execution only' services
- B The inability of clients to find an adviser who will charge an appropriate level of commission
- C The gap between the industry's expectations and those of the FCA
- D The inability of clients to find the advice they require at a price they can afford

4. Which one of the following criteria does not form part of the assessment of being fit and proper?

- A Years of service in regulated activity
- B Honesty and integrity
- C Qualifications held
- D Role experience and training

Access to *Professional Refresher* is available on an annual licence basis. The full suite of modules is free to CISI members or £250 for non-members. If you or your firm would like to find out more about *Professional Refresher*, visit cisi.org/refresher or contact the CISI on +44 20 7645 0777.

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Update to the CISI Code of Conduct

With this edition of *The Review*, you will find an updated copy of the CISI Code of Conduct.

The Code seeks to ensure that CISI members adhere to the highest ethical standards at all times. It sets out the behaviours expected of CISI members and provides guidance to those who find themselves faced with an ethical dilemma. The Code is regularly reviewed by the Integrity and Ethics Committee, which recently recommended some updates to it.

First, the Introduction to the Code now prompts members to ask themselves four simple questions to determine the best course of action when faced with making a decision, where the most suitable choice is not immediately

obvious: is the course of action you are considering honest, open, transparent and fair?

Second, two of the Principles have been slightly revised following the merger of the CISI and the Institute of Financial Planning (IFP) in 2015. This has been done to reconcile the CISI and former IFP Codes. As a result, Principle 1 now includes the importance of putting the client and customer first, and Principle 4 includes confidentiality in the standards required when engaging in any form of market dealings.

Finally, the revised Code notes that duties are owed by members to specific stakeholders, and shows examples of the stakeholder(s) most closely associated with each Principle.

CISI Financial Planning Gala Awards

In October, the CISI celebrated the outstanding achievements of financial planners and firms at the Financial Planning Gala Awards. We spoke to the prize winners about their accomplishments

The CISI held its first ever Financial Planning Conference, themed ‘Stand tall together’, at the Celtic Manor Resort in Newport, Wales, on 3–5 October 2016. More than 450 delegates, speakers, exhibitors and sponsors gathered for personal and business development opportunities, quality structured CPD, the sharing of best practice, catching up with friends and making new connections.

The Financial Planning Gala Awards were held on the second evening, in recognition of the outstanding achievements of individuals and firms across the UK financial planning profession. Charlotte Hawkins, presenter of *Good Morning Britain*, hosted the ceremony,

handing out a total of eight awards to the winners featured over the next few pages.

In recognition of everyone who participated in the process, CISI Head of Financial Planning, Campbell Edgar CFP™ Chartered FCSI said: “The wonderful thing about a conference which incorporates an awards dinner is the inclusivity. While we recognise the success of the winners, we should also recognise and congratulate all of the entrants, in particular the finalists, those shortlisted, who have to go the extra mile in the weeks leading up to the conference, in preparing their entries, presentations and submissions, all of which takes time and effort.”

Award winners

LIFETIME ACHIEVEMENT AWARD

Paul Etheridge MBE CFP™ Chartered FCSI

The Lifetime Achievement Award was handed to Paul (pictured centre) in recognition of his contribution to the financial planning profession and the Institute of Financial Planning



(IFP), which he formed in 1987 and which merged with the CISI in 2015.

How do you feel about winning the award?

It was totally unexpected but I really appreciate it, and it sums up the Institute’s successes over the years. We are stronger now than we have ever been, and the future is looking very bright for the financial planning profession. There are so many amazing opportunities out there.

What did you think of the Financial Planning Conference?

I enjoyed it very much. As at all previous conferences, it provided excellent opportunities to increase my knowledge, to meet old friends and to make additional ones.

Read our interview with Paul in the September issue of The Review (pp.25–26) or at cisi.org/pauletheridge

THE TONY SELLON MEMORIAL PRIZE ‘GOOD EGG’ AWARD

Jane Wheeler, Chartered FCSI

Awarded in recognition of contribution to financial planning, following nomination by CISI members.

Jane said: “I have recently retired and was absolutely delighted to be awarded this in recognition of my contribution to the IFP and the profession in general. As I step away from it all, I fervently hope that members will support the CISI as it continues the excellent work begun by the IFP so that real financial planning may be available for the benefit of more consumers over time.”



ACCREDITED FINANCIAL PLANNING FIRM™ OF THE YEAR

Acumen Financial Planning

The award recognises the firm that has made the strongest impact on the financial planning profession over the past 12 months. We spoke to the managing director of Acumen Financial Planning, Sandy Robertson CFP™ Chartered FCSI (second from right).

How do you feel about winning?

Immensely proud and delighted. The whole team at Acumen Financial Planning work extremely hard to provide clients with the best possible service, together with a clear vision of their current and future financial affairs. To be recognised for this, and our ongoing contribution to the financial planning profession as a whole, is a huge accolade for the team.

What feedback did you receive about why you won the award?

Campbell said it was difficult to choose between the shortlisted firms, but:

“In the end it was a matter of balance between the presentations made, the responses to the questions asked and the panel reviewing their judgments in the light of the criteria given.

“All three firms are excellent and the panel was in the invidious position of having to decide a *primus inter pares*.”

Applicants were required to submit 2,500 words on the impact that their firm had made to the financial planning profession over the past 12 months. Could you sum up that response in a couple of sentences?

We have always focused on providing the best possible service for our clients through our people and our processes. In order to do this, we ensure our team has the support to be at the top of its area of expertise and our processes are finely tuned to manage a significant workflow without compromise to service levels.

Finalists for the award

Carbon Financial Partners
Mazars



PARAPLANNER OF THE YEAR

Jenny Ryan, Paraplanner at Baigrie Davies

Awarded in recognition of the broad range of skill levels and abilities paraplanners have. Jenny (right) did not attend the ceremony so IFP Forum Chairman Ian Howe CFP™ Chartered MCSI accepted the award on her behalf.

What feedback did you receive from the judging panel about why you won?

I got some really lovely feedback. They said that they could see I put the client at the heart of everything we do. It's always nice to get validation from people who work in the same field as you.

What made you decide to enter the competition?

I went to the CISI Paraplanner Conference earlier in the year, and they were encouraging people to give it a go, and I thought, ‘Why not?’

Which essay did you decide to do: ‘What is a paraplanner worth’ or the ‘Three-year training programme for a trainee paraplanner’, and why?

The first one. I wrote about how a paraplanner is worth their weight in gold, and worked out what the gold price was on the day. I wanted to do something that was a bit fun because I thought it might catch the eye of the judges, and it seems to have worked!

Finalists for the award

Mohamad Alrayees
Andrew Haley
Farida Hassanl



“It’s always nice to get validation from people who work in the same field as you”

THE JONATHON TIMMS MEMORIAL PRIZE

James Lee CFP™ Chartered MCSI

Awarded to the candidate with the highest result for the CISI Diploma in Financial Planning to meet the CFP™ certification standards in the year.



How do you feel about winning?

Passing the case study assessment already felt like a great achievement, and the recognition of the award gave me a real sense of confidence in the way that I had approached the assessment and my financial planning in general.

What advice would you give to someone taking the qualification? Do you have any tips for aspiring financial planners on how to pass the financial plan component of the diploma at first submission?

My initial advice would be to utilise the CISI resources that are available. The Case Study Preparation course was fantastic and really helped me to structure my approach. My main tip would be to resist the temptation to jump straight into thinking about solutions – spend time getting to know the case study and the client. I created a mind map using photos of someone the same age as the client and mapped out the entire fact find and soft facts on to one A3 page. This helped me to

bring the case study to life as I could picture the client's entire situation.

Would you recommend this qualification to others?

Without a doubt. I passionately believe in financial planning, and working with clients to build a robust plan is vital and makes such a tangible difference to people's lives. Studying the qualification has been a real catalyst for change in the way I approach clients and has pushed me to identify gaps in my own learning and knowledge and has certainly made me a more rounded financial planner.

“The recognition of the award gave me a real sense of confidence”

MOST EDUCATIONAL STAND AWARD

Winton

MOST INNOVATIVE AND CREATIVE EXHIBITION STAND

Winton

Delegates voted Winton as the winner of two exhibition stand awards for innovation and education. We spoke to Charlotte O'Horo, associate at Investment Solutions, Winton (pictured second from right, with colleague Abigail McTear, associate in investor services, Winton).

How do you feel about winning both awards?

Delighted. It was nice of the CISI to include awards for the sponsors. It helps make the sponsors feel part of the event and encourages them to make an effort next year, which will be for the benefit of the delegates. But ultimately of course the annual conference is about celebrating and recognising outstanding financial planners, and the positive impact they make to their clients.

What feedback did you receive about why you won the Most Educational Stand Award?

Our approach to investing differs from mainstream competitors. Winton uses the scientific method to analyse and find patterns in big data. As such, many of the topics and strategies we were discussing with delegates were new and interesting to them.

What feedback did you receive about why you won the Most Innovative and Creative Exhibition Stand Award?

Most of the delegates who came to visit our stand commented on the effort we had put into its design and layout. The more interactive and interesting stands help to increase delegates' overall conference experience. The educational quiz on the large plasma screen display was also fun and popular.



“The more interactive stands help delegates' overall experience”

TRANSACT: ADVISER- FOCUSED TECHNOLOGY

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Transact is the UK's longest-running independent platform, having been first to market in 2000. Over the years, our business principles have remained the same: to be adviser-focused, flexible and transparent in all our dealings.

Our solutions are designed to make advisers and their clients' lives easier, and adviser businesses more efficient. Advisory professionals have rated Transact as the 'Best overall platform' in both the CoreData Investment Platform Study and Investment Trends Adviser Technology Report from 2010 to 2016.

We continue to collaborate with a wide range of third parties to help advisers in their work, with access to:

- over 80 discretionary investment managers
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- all the major back-office systems
- cashflow modelling tools (eg, CashCalc and Truth)

- a developing trust proposition with access to a range of trust service providers.

We own our own platform technology, so can respond quickly to industry change and provide monthly platform updates.

Transact is a truly sustainable platform. We currently administer over £25bn of funds in more than 133,000 client portfolios, and in our 2014/15 financial year achieved profit of £20.8m (before tax).

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Royal London

www.adviser.royallondon.com

Schroders Investment Management

www.schroders.co.uk/adviser

Corporate Members

Aegon www.aegon.co.uk

AIC www.theaic.co.uk

Alliance Trust Savings

www.alliancetrustsavings.co.uk/adviser

Aviva www.aviva.co.uk

Dimensional Fund Advisors

www.dfauk.com

IRESS www.iress.co.uk

Just Retirement www.justadviser.com

Morningstar www.morningstar.co.uk

NS&I www.nsandi.com

Parmenion www.parmenion.co.uk

Partnership www.partnership.co.uk

Prestwood Software

www.prestwood-group.co.uk

Seven Investment Management

www.7im.co.uk

Standard Life www.standardlife.co.uk

TIME Investments

www.time-investments.com

Transact www.transact-online.co.uk

Vanguard www.vanguard.co.uk

PARMENION: TECHNOLOGY TO SUPPORT A UNITED PROFESSION



At Parmenion we have been a proud, long-standing sponsor of the IFP, and judges of the Paraplanner of the Year Award, now awarded by the financial planning team at the CISI.

Founder Richard Mein was for many years a private client stockbroker with J Edward Sellars in Bristol. He saw the potential to deliver great investment outcomes to clients working with advisers by applying the key ideas in modern portfolio theory to drive professional asset allocations into discretionary fund-based portfolios. The Retail Distribution Review and the FCA's drive towards improved advice suitability has seen Parmenion grow to managing over £2.7bn for retail investors.

Those monies are spread across an extensive range of diversified portfolios, including those for clients looking for different investment styles, including ethical investment, high income and, notably, income drawdown. As the market for pension drawdown grows, with fewer and fewer salaried professionals in defined benefit pension schemes, the flexibility of Parmenion's technology will take on greater significance. The ability to deliver a

high-quality pension portfolio service, managed by professional wealth managers, will be exploited more and more by CISI firms, old and new, addressing this important market opportunity.

By way of illustration, the Parmenion self-invested personal pension has possibly the widest range of withdrawal options on any platform, including Uncrystallised Funds Pension Lump Sums, and bears no additional wrapper cost.

The vision is not only to see a profession united around common examination routes and professional standards, but also one in which the operating technology supports superior service levels and value for money. This will allow true investment management expertise to be leveraged with larger numbers of clients, even those with relatively straightforward needs and more modest investment sums.

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Ask the experts: Getting ready for the Fourth Money Laundering Directive

The HM Treasury (HMT) consultation on the UK's implementation of the EU's Fourth Money Laundering Directive (4MLD) has closed recently. Which particular features should CISI members be aware of?

First, members should start planning how they are going to implement 4MLD. Notwithstanding Brexit, the UK Government is required to have 4MLD on the statute book and have it implemented by 26 June 2017. Second, I would recommend that members become aware, if they are not already, of the Directive's requirements and the issues on which HMT consulted. I believe it is highly unlikely that many requirements will substantially change as a result of the consultation.

A key feature of any anti-money laundering (AML) controls is customer due diligence (CDD). Which CDD changes should members consider?

4MLD reinforces the risk-based approach (RBA). In the Directive's annexes there are non-exclusive lists of lower and higher risk factors, which firms should review. The Directive now requires firms to conduct risk-based CDD on all existing clients. Much to the chagrin of solicitors, pooled client accounts are no longer automatically deemed to be lower risk. Firms will have to consider how to treat such accounts in the future.

“The Directive requires risk-based CDD on all existing clients”

Are there any changes to the provisions on reliance?

Generally, firms cannot now rely on entities based in higher risk third countries. However, 'financial and credit institutions' (ie, banks) will be permitted to rely on units based in such countries within their own corporate group only if there is effective implementation of group AML

policies. HMT has asked whether banks should be able to rely on other entities in these countries. Banks should track how HMT resolves this issue.

Are there any new requirements on systems and controls?

Consolidating the RBA, "where appropriate" firms will need "an independent audit function" to test their AML controls. Whether internal audit teams are deemed independent is currently undecided. Also, "where appropriate", firms must now screen employees. Members should track whether HMT issues any guidance on these issues.

Politically exposed persons (PEPs) frequently feature in AML 'war stories'. Are any changes envisaged to PEPs?

4MLD brings domestic PEPs within the PEP definition, as are members of the governing body of any political party. With over 400 parties registered with the Electoral Commission, firms will have to decide whether to cover all the parties or, perhaps, just those who have members in the Westminster Parliament and the devolved assemblies. HMT opined that domestic PEPs should be treated "at the lowest level" of enhanced due diligence. Finally, following the recent scandals at FIFA and other sports bodies, HMT is considering bringing "senior members of international sports federations" within the PEP scope.

I've heard something about a fifth Money Laundering Directive (5MLD). Can you elaborate on this?

Following the Paris attacks and the publication of the Panama Papers, the European Commission decided to strengthen 4MLD by January 2018. There are proposals to reduce the anonymity of e-money and stored value cards. Also, it is proposed that each member state has a national register of bank and payment accounts that would be open only to the authorities, just as they are in France and Germany. The register

would include the account number, the identity of the account holder (and any beneficial owners) and an identifier, such as a National Insurance or passport number. Details of balances and transactions would not be maintained on the register. Additionally, for some non-trading companies, beneficial ownership requirements and transparency would be lowered from 25% to 10%. Public registers of the beneficial owners of corporates will become mandatory. Finally, financial intelligence units will have the authority to demand information from firms in cases where firms have not submitted a Suspicious Activity Report.

“Members would be well advised to follow these developments”

Do you have any final advice to members?

Members should track how HMT decides to implement 4MLD and the progress in Brussels of 5MLD. By June 2017 the European Supervisory Authorities will be issuing guidance on 4MLD. The Joint Money Laundering Steering Group (JMLSG) in the UK will update its guidance for firms in due course. There's also the Criminal Finances Bill in Parliament to monitor. So members would be well advised to follow these developments and plan how they are going to implement all these new requirements as well as doing their day job!



Denis O'Connor FCSI has held senior financial crime roles in various institutions. He was also a member of the JMLSG Board and its Editorial Panel from 2010 to 2016

BACK STORY

*Adam Greaves MCSI,
investment manager,
Brooks Macdonald*



In summer 2016, Adam Greaves MCSI was listed in *Citywire's* 'Top 30 under 30' in the UK wealth industry for the second year in a row – proof that his time at Brooks Macdonald, which he joined in 2013, has been successful. "It goes without saying it is an absolute privilege to be included," he says. "I couldn't be more appreciative that our small island of Jersey in the Channel Islands is gaining traction, and for the acknowledgement of the top-class personnel we have in the island."

Both Adam's parents worked in financial services and he says it was always an area that attracted his attention. "I completed my A-Levels in Business Studies and Accounting (along with Maths and Further Maths), and then studied Management Sciences with Accounting at the University of Southampton, so it was a natural move, and one I wouldn't wish to change."

“I have always had a keen interest in my own personal investment portfolio”

Adam spent the first five years of his career at EY as an audit executive. "I decided it was opportune to move into asset management," he explains. "I have

always had a keen interest with regards to my own personal investment portfolio, and completed my benchmark investment qualifications while at EY."

He and his team are focused on the African market, travelling regularly to the continent to service the independent financial adviser and professional intermediary communities. And there are plenty of recent developments to keep them on their toes: "South Africa is currently going through the Retail Distribution Review, which the UK went through in 2013. We are using our experience to provide support via education to the South African intermediary market and gaining traction through transparent fees and clear segregation of duties in providing suitable advice and investment services."

For such a short career, Adam has plenty to shout about, but he says he is most proud of his professional development: "I consider my biggest achievement to be the progression I have made in the three years from my accounting days to where I am today at Brooks Macdonald. As an investment manager, I oversee and manage in excess of £400m, but alongside that have also passed all three CISI Chartered Wealth Manager modules at the first attempt with two passes and a merit.

"Being a member of the CISI has meant a great deal in regards to reputation and acknowledgement from like-minded industry professionals who appreciate the hard work entailed."

Events preview

The CISI offers plenty of opportunities to help you meet your requirements for professional development. Below are just some of the highlights of the Institute's events programme, but for comprehensive details and to book, please visit cisi.org and click on the 'Networking & events' section.

CONFERENCES & GALA

19 JANUARY

CISI ANNUAL INTEGRITY DEBATE

Plasterers' Hall

Our annual debate will focus on whether it is up to challenger banks or established banks to rebuild consumer perception of the City. One not to be missed.

13-14 JUNE

PARAPLANNER CONFERENCE

Oxford

We are hosting one of the largest conferences for paraplanners which will focus on a mix of technical and soft skills.

CPD WORKSHOPS

26 APRIL Protection

24 MAY Retirement

ANNUAL DINNERS

20 JAN Guernsey Branch Annual Dinner

2 FEB Northern Ireland Branch Dinner

22 FEB 25th Anniversary London Annual Dinner

4 MAY Liverpool, Chester & North Wales Branch Dinner

OTHER HIGHLIGHTS INCLUDE

10 Jan 2017: The new market abuse landscape (London)

23 Jan 2017: Leadership precepts for teams that work (London)

24 Jan 2017: Answering the 'when' question using modern technical analysis (Guernsey)

25 Jan 2017: Pensions – impact of recent (2015) changes to the pensions planning landscape (Leeds)

26 Jan 2017: From property to private equity: Accessing illiquid assets through liquid vehicles & Risk and cyber security culture (Norfolk)

26 Jan 2017: Passive solutions for sustainable investing (London)

16 Feb 2017: ETF liquidity and the mechanics of trading ETFs (Guernsey)

21 Feb 2017: Angela Knight – Financial services – big pay and shady deals or an essential profession? (Leeds)

IN-HOUSE TRAINING

The CISI delivers in-house training courses for members and non-members, spanning a variety of skill areas. If you have a team that requires training, please contact Alex Xavier (assistant director, member services) on +44 20 7645 0725 or alex.xavier@cisi.org

• If you have an idea for an event or would like to contribute at one of our events, please email cpdevents@cisi.org

Technology could kill the ‘company’

IT MAY BE TIME FOR TRADITIONAL COMPANIES TO RETHINK THEIR STRUCTURE IF THEY ARE TO SURVIVE THE COMPETITIVE ONSLAUGHT FROM TECHNOLOGY-DRIVEN RIVALS

✦ ANTHONY HILTON ✦ JOHANNA WARD

The world’s biggest taxi company does not own any taxis. That’s Uber. The world’s biggest retailer, Alibaba (not Amazon), does not own any shops. The world’s biggest media company, Facebook, does not generate any content. The world’s biggest hotel company, Airbnb, does not own any hotels. What’s more, none of these businesses existed 20 years ago. Meanwhile, the management consultancy firm McKinsey has suggested that such is the pace of change that 35% of the business models currently in use in today’s companies will be obsolete within five years.

Technology companies look at the world differently and that is why it is so hard for established businesses to compete with them. Company boards say they want to innovate but in truth, while senior management does, and a few young ambitious individuals anxious to make their name certainly do, the vast majority of employees in an organisation are usually quite comfortable with the status quo. They understand it, they are on top of what is expected of them, they are not threatened by it and they know how to turn it to their advantage. So as long as the business is not visibly collapsing around them, why would they want to change?

Innovation to them is a threat, however much others in the business may think of it as an opportunity, and as a result, middle-ranking employees resist change, not with overt challenge because that might get them fired, but with minimal co-operation, which amounts to passive resistance. This gradually saps the will of the would-be innovators who are normally vastly outnumbered by the incumbents. The project stalls, the glamour fades and the limited attention span of the chief executive means the organisation moves on to something else.

It is an exaggeration to say that an existing company is more likely to go to the wall than to evolve, but that is the way things are moving. The FTSE 100, which represents the largest companies listed on the London Stock Exchange, has lost 90% of its founding members in 30 years.

Even if today’s businesses are not universally doomed to fail, it seems not unreasonable to suggest that we will have to rethink the way they are run.

There are two issues. First, the need to capture and evaluate even the smallest but potentially crucial piece of market information seems to demand a flat,

networked structure where information flows freely in all directions. The traditional command-and-control hierarchy, where information goes only up or down and frequently gets stuck, will simply not be responsive enough.

Second, human resource experts say we are moving towards a world where there are few full-time employees, but people come together to execute specific projects. The usefulness of tomorrow’s human resources manager lies in knowing what skills are going to be needed to execute a strategy and knowing where they might be found.

The point is that we are entering a world where the scarce resource is labour, not capital. There is more than enough money around to back new ideas; more so because today’s businesses require a tiny fraction of the capital demanded by yesterday’s corporate giants. It is people who are in short supply – and specifically people with the skills and understanding to harness the power and opportunity of today’s technology.

But this raises questions about the purpose of the corporate structure. The modern limited liability company is a capital preservation device; a legal structure designed almost exclusively to protect the interests of those who provided the capital. It reflects an age when capital was the scarce resource. But if capital is no longer the scarce resource, why persist with a business structure that still assumes that it is?

The traditional model for a business that needed talent but no capital was the partnership and it may be that it will experience a renaissance. Alternatively, something akin to a legal chambers might have other applications – umbrella organisations where people who are virtually sole practitioners come together to share a few overheads and clerical services but keep the bulk of what they earn.

Perhaps the biggest victim of the coming technology storm will be the company itself.

Anthony Hilton is the award-winning former City editor of *The Times* and the *London Evening Standard*





iStock

The year ahead

2017 LOOKS SET TO BE A YEAR OF PREPARING FOR KEY PIECES OF REGULATION, PEPPERED WITH A GOOD DOSE OF POLITICAL UNCERTAINTY. WE TAKE A LOOK AT WHAT FINANCIAL SERVICES PROFESSIONALS AND FIRMS SHOULD EXPECT

◆ EILA MADDEN



President Donald Trump takes office

As if there wasn't enough political uncertainty in 2016, 2017 is set to offer up another 12 rollercoaster months. First up is Donald Trump's inauguration on 20 January. Uncertainty about how Trump will govern will abate in the new year, but the steadiness of markets will depend upon the steadiness of Trump's hand on the tiller.



NS&I offers savers some good news

Government-owned National Savings and Investments (NS&I) launches a three-year savings bond, offering a

2.2% interest rate. Open to anyone aged 16 or over, savers can make a minimum investment of £100 and a maximum of £3,000.

The SMCR broadens its reach on boosting individual accountability

The Senior Managers and Certification Regime (SMCR) calls for all certified individuals to be assessed as 'fit and proper' by March 2017. The regime's high-level conduct rules will also apply to nearly all staff (bar ancillary staff) by this date.

In 2018 the SMCR will be extended to apply to all firms authorised under the Financial Services and Markets Act 2000. The FCA intends to consult on rolling out this extension in 2017 (see page 37 for more).

Elections in Hong Kong and France

Hong Kong elects a new Chief Executive in March. Pro-democracy protestors could be

on the move again if they perceive the elections, overseen by Beijing, to be undemocratic. Jitters on the Asian markets are likely to spread west. Europe will wait to see if Marine Le Pen, leader of the far right Front National, takes the Élysée Palace. A political upset like that could see France taking a more protectionist approach to issues such as trade and employment, putting the European project at greater risk.

Britain triggers Article 50

UK Prime Minister Theresa May has pledged to trigger Article 50 to begin Brexit negotiations with the EU in March. Investors will enter a two-year period of uncertainty while they await the outcome (see page 37 for more).



Enhanced ISA options for savers

The £15,240 annual ISA allowance will rise to £20,000. In addition, a new Lifetime ISA (or LISA) will come onto the market to help the under 40s save for their first home or for retirement. LISA savers, who have to be 18 to 40 when they open the account, can save up to £4,000 a year and, at the end of each tax year, will receive a state bonus of 25% of what they have saved that year. The bonus will be paid until the saver reaches 50.

More generous inheritance tax (IHT) rules come into force

April sees the introduction of the new IHT Residence Nil Rate Band (RNRB), which will allow individuals to pass on up to an additional £175,000 of the value of their main residence, as long as it goes to direct descendants. The new allowance will be phased in over four years, starting with a £100,000 allowance in 2017/18.

Landlords lose higher rate tax relief

Buy-to-let landlords who are higher or top rate taxpayers have traditionally received tax relief of 40% and 45% respectively. From April, this starts to get phased out over a four-year period, to be replaced with a flat rate of 20%.

Apprenticeship levy hits firms with a £3m-plus pay bill

On 6 April 2017 the UK Government's apprenticeship levy will come into force. This requires all firms operating in the UK, and with a wage bill of more than £3m, to invest in apprenticeships by contributing to a central funding pot.

The levy is 0.5% of a firm's total pay bill, minus a £15,000 allowance.

Mandatory Gender Pay Gap Reporting – preparations should start this year

Another set of rules due to come into force on 6 April 2017 is the Equality Act 2010 (Gender Pay Gap Information) regulations. They will require all private and voluntary sector employers with more than 250 employees to publish information about the gender pay gap in their organisations.

Results of the first gender pay gap analyses are due to be published in April 2018 and will cover the period from May 2016 to April 2017. That means firms should begin collecting data from April 2016 and should start to carry out their calculations from April 2017.



Iran votes

Iranians vote for a new president on 19 May. If reforming incumbent Hassan Rouhani fails to get re-elected, his deal with the UN and EU to curb Tehran's nuclear ambitions in exchange for the lifting of economic sanctions could be under threat. Hardliners in Tehran are opposed to Rouhani's reforms and if they take back control, it could lead to a re-imposition of sanctions.



Fourth Anti-Money Laundering Directive triggers AML training review

The fourth EU Anti-Money Laundering Directive will be implemented in all EU member states by 26 June 2017. This brings in new customer due diligence checking requirements and new obligations to maintain a record of payments and report suspicious transactions, among other measures. Anti-money laundering training is a legal requirement for all financial services firms. Changes to the law should trigger reviews of existing training provision and the need for refresher training courses (see page 13 for more).



MiFID II brings more companies and products into its net

MiFID II will expand the scope of the original Markets in Financial Instruments Directive

to cover a greater number of companies and products, and include fewer exemptions. Member states must adopt measures to transpose the revised directive, which takes effect from January 2018, into domestic law by July 2017. During 2017, financial services firms will need to dedicate significant resources to prepare for MiFID II. Preparations will need to include extensive training programmes to ensure employees are familiar with the changes and their potential impact (see page 37 for more).

Uncertainty about how Trump will govern will abate in the new year

Regulation on KIDs and PRIIPs

The Packaged Retail Investment and Insurance-based Investment Products (PRIIPs) regulation introduces a standardised fact sheet, also known as a Key Information Document (KID), which is designed to present the main features of an investment product in a simple and accessible manner. A regulatory framework should be in place in the first half of 2017 and apply as of the beginning of 2018.



German election tests Merkel's popularity

Although Angela Merkel is still on course to be re-elected, anger over her handling of the European migrant crisis means she can't take victory for granted. As in France, a more inward-looking German Chancellor could further threaten the EU.



GDPR could be costly for firms

The General Data Protection Regulation (GDPR) intends to strengthen and unify data protection for individuals within the European Union. The most significant change is the need to obtain freely-given and auditable customer consent for the processing of personal data. Firms could be fined up to 4% of global turnover for non-compliance. The rules were adopted in April 2016 and come into effect on 25 May 2018. Firms will need to start getting to grips with the new requirements during 2017.

DEPARTURES OF CLIENT-FACING ADVISERS FROM A FIRM CAN BE ACRIMONIOUS, AS EMPLOYERS WORRY ABOUT CLIENT POACHING. HOW CAN COMPANIES HOLD ON TO BUSINESS AND ALLOW ADVISERS TO LEAVE ON GOOD TERMS?

HEATHER CONNON ANDREW BAKER

Changing places



Who owns a client? That may seem like a strange question: clients are surely free to put their business and their funds wherever they like. But when a client-facing employee, such as a financial adviser, planner or fund manager, moves from one company to another, it can become a hotly disputed subject. The old employer will be keen to ensure that it does not lose any business as a result of the staff move; the adviser will want to take as much business as possible to the new employer; in the middle is the client, who will have their own opinions on which is the most important relationship.

Contracts will often include a requirement that the employee serves ‘gardening leave’

Employers will generally try to pre-empt disputes by putting in place employment contracts setting out rules their employees must observe if they move firms. Contracts will often include a requirement that the employee serves out notice on ‘gardening leave’, which means they will still be paid and employed by the firm, but will not be allowed to come into the office. The aim is to give the existing employer time to choose a successor and reassure clients that there will be no change in service. Many contracts will also have restrictive covenants, which aim to prevent leavers taking any business from the firm.

WHEN ADVISERS LEAVE

Steven Cochrane, a partner specialising in employment law at Pinsent Masons, says there are four main types of restrictive covenants. The first, and most draconian, is a non-compete clause, which prohibits an employee from joining a competitor. The second is a non-solicit clause, which prevents the employee approaching clients and asking them to move to the new firm. Because non-solicits can be circumvented by a client moving of their own volition (with no demonstrable solicitation by the



employee), some employers also augment employment contracts with a non-dealing clause, which prevents employees from accepting business from former clients for a predetermined period. The fourth, a non-poaching clause, is intended to stop a departing employee taking other members of staff to the new company. In all these cases, the restriction is typically in place for six to nine months, with any period spent on gardening leave normally being offset against the post-employment prohibited period.

“The more draconian clauses in a contract are, the more difficult they are to enforce”

Writing a restrictive covenant is simple enough; enforcing it can be far less straightforward. “As a general rule, they can only be enforced if they go no further than is reasonable to protect the former employer’s legitimate business interests,” says Steven. “The more draconian they are,

the more difficult they are to enforce. Non-compete clauses are the most difficult to enforce; the other three are generally easier to establish as reasonable, but the devil is in the detail and it is crucial to draft carefully, having regard to the specific scenario.”

Disputes are not uncommon, although the huge expense and time needed to pursue a case means they rarely go all the way to court, he adds. Instead, companies will usually try to settle disputes with a pre-action cease and desist letter reminding the departing employee of the contractual clauses. Given that restrictive covenant enforceability is never an exact science and there is almost always scope to argue for and against, it is often the case that the former employee will instruct a solicitor who will in turn contend that the restrictions are unreasonable and unenforceable. Often this leads to a negotiation with a view to both sides agreeing on a mutually acceptable middle ground.

CLIENT CONCERNS

But what about the opinions of clients? They will generally not be aware of restrictive covenants preventing them moving with their adviser, and may be shocked and upset when these come to light. David Hazelton, head of business development at wealth manager Raymond James Investment Services, thinks that needs to change. “We think that, at a minimum, clients should be made aware in the firm’s terms of business statement of the existence of these clauses in advisers’ employment contracts. That would give greater clarity and allow clients to make better informed decisions if they object to the restrictions.”

In fact, he adds, some firms will not force clients to remain against their will, allowing those who write to complain to follow their adviser to the new company regardless of any non-dealing clauses. Those without the time, or knowledge, to do so may be forced to wait until the non-dealing period has elapsed, or to work with a different adviser if they move their business to the new company ahead of time. “The fact that clients are prepared to write and complain is a sign that they are not happy with this situation,” David says.

“At a minimum, clients should be made aware of the existence of clauses in advisers’ contracts”

His own firm makes it clear that clients can move with their adviser, but also emphasises to any adviser joining the firm the importance of understanding any legal requirements in their old employment contracts and the dangers of breaching them. This understanding was one of the factors that helped seven advisers who joined Raymond James after leaving financial advice and investment firm Edward Jones, in preference to being acquired by Towry, to win a legal action. They claimed Towry had breached anti-solicitation clauses in their contracts. It was, the court held, clear that the clients were loyal to their advisers and preferred their service to that offered by Towry.

Head of Policy Strategy Development at the Tax Incentivised Savings Association Peter Smith adds: “Actually, the client owns the client; they will make the decision about which adviser they use at the end of the day.” His organisation has been working



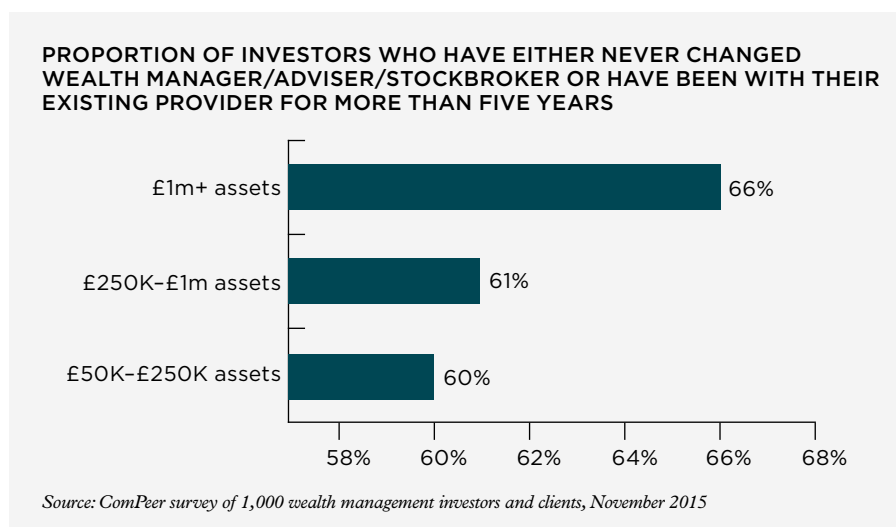
with financial services companies to draft a voluntary protocol for employment contracts to minimise the risk of disputes when advisers move firms, although it is not clear how widely that has been adopted. A similar protocol is widely used in the US, where it was initially drafted by a handful of firms who wanted to stop the expense of constantly suing each other and subsequently adopted by others. However, the client is already pre-eminent in the US advisory process: non-dealing covenants are prohibited and many states also outlaw non-solicitation clauses.

“Clients will make the decision about which adviser they use at the end of the day”

The UK’s Financial Conduct Authority has not generally taken an interest in this area, and it is likely that the regulator would regard any dispute as a private issue between companies and their employees. But Pinsent Masons’ Steven says that employers who are keen to uphold restrictive covenants may be able to use the regulatory requirements of a CF30 client-facing employee to help: “There is a fit and proper test; they have to be deemed fit and proper having regard to honesty, integrity and reputation.” It is at least arguable that engaging in unlawful conduct in breach of post-termination restrictions could go to an individual’s honesty and integrity and, as such, former employers may, in addition to pursuing contractual claims, regard breaches as a wider regulatory issue.

STAR MOVES

If the departing employee is a fund manager, the company will have little or no control over what happens to clients’ money.



Indeed, the more high profile and successful the manager, the more cash is likely to follow the manager out the door. PIMCO lost more than \$120bn in the year following the departure of its star fund manager Bill Gross in 2014; Invesco Perpetual saw £2bn withdrawn from funds managed by Neil Woodford when he left to set up his own business. Analysts and advisers will often put their fund recommendations on hold following the announcement of a manager’s departure, and may advise switching to a rival, or following the manager to their new firm. It can take years before it is clear whether the new managers will be as good as those they replaced – and whether the departing manager can continue to work their magic at the new company.

Analysts at Moody’s, the rating agency, cite three key situations that heighten the risk of a manager’s move having a significant adverse impact on the company: founders of companies who built the franchise on their

own; star managers who oversee a substantial amount of the firm’s assets; and principal stakeholders who hold a majority of the voting stock. Moody’s says it is vital that companies establish a clear succession policy to reassure investors they are prepared for manager moves, and points to Invesco Perpetual, where Woodford’s departure was well flagged and he had already been working closely with his successor, Mark Barnett.

Invesco Perpetual saw £2bn withdrawn from funds managed by Neil Woodford when he left

“Invesco’s approach to reducing key person risk has been to have a succession plan in place, and to use compensation incentives – such as share-based compensation plans – to retain the potential pool of successors and align their interests with those of the firm. Neil Woodford announced his departure from Invesco Perpetual (UK) in October 2013, and although substantial sums of retail and institutional money flowed out of the firm’s funds, Invesco was able to execute its ‘succession planning strategy’, with Mark Barnett taking on Woodford’s role in May of 2014. The transition was well executed, and involved a long transition period,” Moody’s wrote.

Longer working lives and intense competition for client business means that employment disputes are likely to be here to stay. Companies that foster good relationships with clients, and are proactive in their succession planning, will be well prepared to face these challenges.

BOTH GENERATIONS SEEK A STRONG BRAND AND REPUTATION WHEN SELECTING A WEALTH MANAGER/ADVISER, WITH INVESTMENT PERFORMANCE ALSO IMPORTANT

Top three most important criteria when choosing a wealth manager/adviser	Aged 18-49 ranking it as 1	Aged 50+ ranking it as 1
Brand/reputation of the firm	24%	28%
Investment performance	23%	23%
The level of fees for the services	15%	15%

Source: ComPeer survey of 1,000 wealth management investors and clients, November 2015



Getty

Making a statement

WHILE THE EFFECTS OF PHILIP HAMMOND'S FIRST AUTUMN STATEMENT AS CHANCELLOR MAY NOT SEEM HUGE, THERE'S PLENTY FOR FINANCIAL PLANNERS TO LOOK OUT FOR

✦ TONY WICKENDEN

At the end of November 2016, new Chancellor of the Exchequer Philip Hammond gave his first Autumn Statement. There was, understandably, a strong focus on growth, debt, infrastructure and post-Brexit uncertainty. Hammond (with strong reference to Office of Budget Responsibility (OBR) input) was effectively preparing us for potentially tough times ahead while leaving uncertainty over just how tough they would be. Surprisingly, not every Brexiteer agreed with that basis but that's what the Chancellor is working with.

There was also a reaffirmation of this Government's commitment to being a "Government for all and not the few". So, these fundamental assumptions – increasing debt, economic uncertainty and lower growth – together with a commitment to help so called 'JAMs' (people who are just about managing) influenced the Chancellor's monetary policy. Already more than a few are questioning the extent to which this last commitment has been evidenced by the Autumn Statement proposals.

However, this article will focus on some of the measures announced (and confirmed in the ensuing Finance Bill and accompanying documents) that I believe are of greatest relevance to financial planners. The

Autumn Statement had two key themes: pensions and investments.

Before considering these though, perhaps the most interesting news from the Chancellor's first statement was the announcement that this was to be his last. In future, Budgets will take place in the autumn, allowing changes to be announced well in advance of the start of the tax year. So there will be two Budgets in 2017: the Spring Budget and the first Autumn one. From 2018 onwards there will be a shorter Spring Statement, responding to the OBR forecast, and an Autumn Budget.

PENSION CHANGES

Given the enormous cost of pensions tax relief, the chance of some fundamental change to relief (perhaps moving to a flat rate) was not ruled out. Most, myself included, believe that these changes will be a case of 'when', not 'if'. However, in line with the Chancellor's intention for the Autumn Statement not to be the place for large scale tax changes, pensions were only given marginal treatment. On the other hand, the changes could be quite important to those affected. I am grateful to Sam Kaye and Claire Trott, who lead the Technical Connection pensions team, for the following thoughts on the key aspects of the proposed changes.

MONEY PURCHASE ANNUAL ALLOWANCE

The headline change is the reduction of the Money Purchase Annual Allowance (MPAA) from £10,000 to £4,000 with effect from 6 April 2017. As a reminder, the MPAA is triggered by one of a list of events, for example drawing income from flexi-access drawdown, taking an uncrystallised funds pension lump sum (UFPLS), establishing a scheme pension from a small self-administered scheme (SASS) or by purchasing a flexible annuity.

Why the reduction? If you cast your mind back to when the MPAA was introduced in 2015, the Government said that if it felt that the MPAA system was being abused it would be amended. The abuse comes in the form of an individual investing £10,000, receiving tax relief on the full amount and then withdrawing the £10,000 and only paying income tax on 75% of that amount. Whether or not there has been evidence of the abuse is speculative but there is obviously enough of a concern at the Treasury to introduce the reduction. Consultation on the detail will take place.

Currently, the alternative Annual Allowance is £30,000 (the Annual Allowance less the MPAA of £10,000). It should follow that a reduction in the MPAA means that the

alternative Annual Allowance reduces to £36,000. We will have to wait for clarification as there is no mention of this in the consultation document.

FOREIGN PENSIONS

Somewhat quietly, changes were also announced to the tax treatment of foreign pensions. The fact that the Government is starting to make changes to the tax treatment of monies that have benefited from UK tax relief and been transferred overseas, usually in the form of a transfer to a Qualifying Recognised Overseas Pension Scheme (QROPS), shows that it is taking overseas transfers more seriously. Indeed, HMRC will shortly be holding meetings with the pensions industry to look at QROPS changes with a view to dealing with any unanswered questions that providers and advisers alike have. It sounds potentially ominous so watch this space.

Somewhat quietly, changes were announced to the tax treatment of foreign pensions

The Autumn Statement confirms that the tax treatment of foreign pensions will be more closely aligned with the UK's domestic pension tax regime by bringing foreign pensions and lump sums fully into tax for UK residents in the same way that UK pensions are taxed.

For those individuals that have emigrated and transferred their UK pension funds, which would have benefited from UK tax relief to a QROPS, there will be an extension from five to ten years of the taxing rights of any foreign lump sum payments.

Amends to the Recognised Overseas Pension Schemes list, published by HMRC on 15 November 2016, show a significant cull in the number of overseas schemes meeting HMRC's criteria. It therefore comes as no surprise that there is to be an update to the eligibility criteria for foreign schemes to qualify as overseas pension schemes for tax purposes.

INVESTMENTS

So how about changes proposed in relation to investments? Well, first a couple of relatively targeted and technical changes to offshore funds and dividend distributions to corporate investors and then a few words on venture capital trusts, offshore structures, dividends and savings income and life policy taxation.

OFFSHORE FUNDS

UK taxpayers invested in offshore reporting funds pay income tax on their

share of a fund's reportable income, and capital gains tax (CGT) on any gain when shares or units in their fund are sold or otherwise disposed of.

The Government has announced that it intends to bring in legislation to ensure that performance fees incurred by such funds, and which are calculated by reference to any increase in the fund's value, are not deductible against reportable income but instead reduce any tax payable on disposable gains. This new treatment, which applies from 6 April 2017, will equalise the tax treatment between onshore and offshore funds.

TAX-ADVANTAGED VENTURE CAPITAL SCHEMES (EIS, SEIS AND VCT)

There will be provisions in the Finance Bill 2017 to amend the requirements for the tax-advantaged venture capital schemes – the Enterprise Investment Scheme (EIS), the Seed Enterprise Investment Scheme (SEIS) and Venture Capital Trusts (VCTs) to:

- Clarify the EIS and SEIS rules for share conversion rights, for shares issued on or after 5 December 2016.
- Provide additional flexibility for follow-on investments made by VCTs in companies with certain group structures to align with EIS provisions, for investment made on or after 6 April 2017.
- Introduce a power to enable VCT regulations to be made in relation to certain shares, for share exchanges to provide greater certainty to VCTs.

In addition, a consultation will be carried out into options to streamline and prioritise the advance assurance service.

The Government has confirmed that it will not be introducing flexibility for replacement capital within the tax-advantaged venture capital schemes at this time.

OFFSHORE STRUCTURES

The Government intends to consult on a new legal requirement for intermediaries arranging complex structures for clients holding money offshore to notify HMRC of the structures and the related client lists. It is not certain at this stage what is meant by a 'complex structure'. It is unlikely that this would extend to an offshore bond or fund.

DIVIDENDS/SAVINGS INCOME

A new system of dividend and savings income taxation was introduced on 6 April 2016. No changes were announced in relation to these tax rules in the Autumn Statement. All individuals now receive a tax-

free annual dividend allowance of £5,000. Above that dividends are taxed according to the marginal rate(s) of income tax that an individual pays – 7.5% (basic rate taxpayer), 32.5% (higher rate taxpayer) and 38.1% (additional rate taxpayer and trustees).

All dividend income (including that falling within the £5,000 allowance) will count for the purposes of other tax thresholds; for example, higher rate tax, high income child benefit tax, personal allowance and annual allowance pension taper.

Savers with savings income will be entitled to a personal savings allowance (PSA) of £1,000 (basic rate taxpayers) or £500 (higher rate taxpayers). People who are additional rate taxpayers do not qualify for a PSA. Income within the PSA is taxed at a zero rate – but still counts as income for other tax purposes.

LIFE POLICY TAXATION

Following consultation it has been decided that any policyholder who suffers a chargeable event gain on a part surrender (above the available 5% allowances) that is disproportionately high (taking account of the economic gain in the policy) can apply to HMRC to have the gain reassessed on a "just and reasonable" basis.

CONCLUSION

So, on the face of it, there is very little in the Autumn Statement to cause 'shockwaves' for financial planners and their clients. However, the cumulative impact of the changes described above is not insignificant.

Keeping up with these relatively small developments as they emerge and, where appropriate, factoring them into financial planning decision-making is what enables financial planners to be professional and deliver tangible value to their clients.

• Tony Wickenden is managing director of Technical Connection, a business providing tax, legal and proposition development support and consultancy to financial planners and financial institutions through an online management platform, Techlink Professional. Request a free trial at www.techlink.co.uk. Be sure to indicate that you are a CISI member when prompted to secure a discounted rate if you decide to sign up.

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A woman with voluminous, curly, light brown hair is leaning on a silver metal railing. She is wearing a dark blue, long-sleeved top and a black watch on her left wrist. The background is a modern building with large glass windows and a grid pattern. The lighting is bright, suggesting an outdoor or well-lit indoor setting.

Keep it Simple, Stupid

GEMMA GODFREY, CEO OF ONLINE WEALTH MANAGER MOOLA, EXPLAINS WHY SHE BELIEVES IT'S TIME FOR FINANCE TO CUT OUT COMPLEXITY

✦ DAN MATTHEWS ✎ CHARLIE SURBEY

“People need to take an interest in their finances, but the industry needs to make investing engaging”

GEMMA GODFREY CEO, MOOLA

2001-2004 STUDIED QUANTUM PHYSICS AT THE UNIVERSITY OF LEEDS

2005 GRADUATE TRAINING PROGRAMME AT UBS

2005-2008 FUND MANAGER AT GAM ASSET MANAGEMENT

2008-2012 CHAIRMAN OF INVESTMENT COMMITTEE AT CREDO GROUP UK

2010-2015 SPOKESPERSON FOR THE ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION

2010-PRESENT CONTRIBUTOR AND EXPERT COMMENTATOR FOR ITV, BBC, SKY NEWS, CNBC, AND THE *HUFFINGTON POST*

2012-2015 HEAD OF INVESTMENT STRATEGY AT BROOKS MACDONALD

2015-PRESENT FOUNDER AND CEO OF MOOLA

2016-PRESENT BOARDROOM ADVISER TO ARNOLD SCHWARZENEGGER ON *AMERICAN CELEBRITY APPRENTICE*

Gemma Godfrey wants us all to KISS more. It's the reason she created the finance management online investment service Moola. But don't get too excited. Gemma isn't on a crusade to encourage a spike in lip-locking, she just wants the financial services sector to 'keep it simple, stupid'.

She argues that the language used by professionals is esoteric and hard to understand, meaning barriers to entry feel higher than they should. The net result is that the average saver or investor is habitually confused, and occasionally demoralised, by the lack of clarity.

This, Gemma says, deters people from engaging with financial services, which is a loss to both the industry's businesses and to the thousands of people with spare cash but without a clue about where to put it.

"In financial services, we need to KISS more," she says. "There is a serious lack of keeping it simple. It's about no longer focusing on 'pushing products' and instead solving real customer needs; giving people what they want, in the way they want it.

"Ever since the financial crisis, people have demanded more control over their money, a greater understanding and access. We still have a way to go."

She argues that confusion is a byproduct of an industry that feels it needs to sound smart in order to justify fees. But in a post-credit-crunch environment, success comes from empowering the customer by delivering information in a relatable and engaging way.

INFLUENTIAL EXPERT

The Moola CEO, labelled "the UK's most influential fintech expert" by newspaper *City AM*, argues that a few simple tweaks would make things a lot easier for the average investor. These improvements, combined with a digital interface that allows people to access information about their money in real time, form the bedrock of her online platform.

"There are two sides to this coin," she explains. "Yes, people need to take an interest in their finances to afford all the things they want to in life. But at the same time, the financial industry needs to make investing engaging, with clear guidance to help people to do it."

Gemma's views on financial services have been honed during a stellar career. Despite

having graduated with a first class degree from Leeds University as recently as 2004, she has amassed an impressive level of senior experience, ranging from board positions at major companies to powerful advisory roles and regular commentary slots on Sky, CNBC and the *Huffington Post*.

Between February 2012 and August 2015, she headed up investment strategy at Brooks MacDonald, a publicly listed wealth management business with \$10bn of assets under management. Quick success, she says, comes from hard work and an education based on science, technology, engineering and mathematics (STEM) subjects.

"My father worked in the industry so I grew up with finance and I soaked up the lessons. I went to a good school in north London where pupils were encouraged to test themselves. My friends and I worked hard and I was always just quite driven.

"I did a degree in quantum physics which set me up for a career in finance because you are taught to apply yourself and solve problems. I wanted to get out there and use those skills to do something practical. A STEM background opens doors and doesn't just restrict you to the lab."

"I did a degree in quantum physics which set me up for a career in finance"

A battling spirit and a knack for problem-solving propelled Gemma through her career and continues to do so. On some of her boards she was the only woman and 20 years younger than everyone else; but being the only person fitting her demographic was a source of motivation, not embarrassment.

Today she is pregnant with her second child and, while she is keen to avoid the 'supermum' tag, she is equally determined to plough on with building her business.

Dedication and hard work also explain her media success, she says, which has culminated in a star turn as an advisor to Arnold Schwarzenegger on the US version of TV show *The Celebrity Apprentice*. This, Gemma says, is one of her proudest achievements to date.

"People ask me how I got it and what's the secret. Well the truth is I worked [very hard]. I work so hard to get exposure, it's not like *The Times* or *BBC Breakfast* just falls into your lap. ➔

“I tell them that you have to start small and do every little thing that comes your way. You get up at 5am, you do stuff no one reads, you hone your media skills, you build a network – which changes because people in media move around a lot – and ten years later, bam! It’s true it takes years to be an overnight success.”

If physics is a problem-solving science, then financial advice answers the questions governing people’s everyday lives: how they can grow their money to afford major life costs, such as buying a home, funding children’s education or paying for a wedding.

CONNECTING WITH CLIENTS

The question facing the industry, meanwhile, is how to connect with a wealth of potential clients who are undecided as to where to start.

According to Deloitte figures from 2012, 5.5 million adults in Britain either lack access to a financial advisor or for one reason or another have opted to cease using one. AXA Wealth says the UK has a shortage of financial advisers; just one for every 2,700 people. In the US the ratio is one to 1,400. And PwC says, in a report published in 2013, that about half of the country’s liquid wealth is not invested in products and services offered by banks, wealth managers and independent financial advisers. This equates to about £2tn going begging.

This is the market Moola is tapping into, and Gemma has a track record of connecting with prospective customers via non-traditional means. She has amassed an enormous Twitter following (approaching 55,000 at the last count) that soars above the social media presence of even the most successful fund managers.

It disproves the notion that finance is better discussed behind closed doors and away from prying eyes. Getting the message out there is part and parcel of forcing the industry out into the open where it has room to thrive.

Gemma’s popular TED talk on the subject of KISSing has no doubt helped to swell those numbers, as have regular TV appearances – but why invest so much time and effort in Twitter?

It’s not just a profile, she says: “Social media enables a business to directly engage with their target audience and gather feedback on what it is they’re looking for. It’s a powerful real-time two-way dialogue.”

More generally, digital technology has provided a platform to greatly improve



“It’s true it takes years to be an overnight success”

services in finance across the board. The cost of starting up is lower and new entrants have shaken up the economy in recent years, providing leaner and more relevant products direct to consumers.

“Technology enables businesses to offer services to people they wouldn’t have been able to reach previously, tailored for the way they live their lives,” says Gemma. “Automation reduces costs, so services can be offered for a lower price, opening up access for people while enhancing operational efficiencies and profitability for the firm.”

Digital technology has provided a platform to improve services in finance

Moola was founded in 2015 to capitalise on these changes and disrupt the market. Co-founder Andrew Jordan was previously part of the team that launched VouchedFor, a service connecting investors with top financial advisers.

Part of the motivation for creating the new business came from this experience. Andrew witnessed first-hand the pent-up demand in what he and Gemma identified as an under-served market. Another part is the chance to work with financial advisers (FAs).

A new partnership with technology provider EValue will offer advisers forecasting tools, enabling them to give affordable advice to those who couldn’t stump up the fees before.

“We use technology to reduce the normal overheads and we deal with the whole process for smaller clients, including onboarding, background research and suitability checks,” says Gemma. “We grow the clients and when they get big enough, the FAs can take over.

“We guide them towards a portfolio, they decide whether they want to invest. Then we execute it for them and report back. They can always see details of how well their investments are performing through the online interface.”

Gemma’s business mantra is to ‘solve problems’ rather than ‘sell products’. If you can create something that addresses a latent need, the product will sell itself. In the case of Moola, this means helping people understand how to make their money work harder, which, in the context of the UK’s chronic savings shortage, is tackling a very big problem indeed.

But, fundamentally, it is further evidence of a move towards the ‘service’ aspect of financial services. Customers want more control, easier and greater visibility. Businesses that can provide this will do well in the new environment.



AFTER HITTING A RECORD LEVEL IN 2015, INVESTMENT IN GREEN ENERGY IS LIKELY TO HAVE DROPPED IN 2016 IN THE FACE OF CUTS IN GOVERNMENT SUPPORT. AS A RESULT, THE RENEWABLE ENERGY INDUSTRY NEEDS TO RETHINK ITS APPROACH

◆ DOMINIC DUDLEY

Green revolution

Energy is an investment-heavy industry. In the UK, it accounts for 2.5% of GDP, but 12% of total investment, according to the Department for Business, Energy & Industrial Strategy (BEIS). The potential for large investment was highlighted when the Government decided to go ahead with the £18bn Hinkley Point C nuclear plant in September 2016.

When it comes to renewable energy, the figures are also large. According to Bloomberg New Energy Finance (BNEF), a record \$23.4bn (£15.2bn) was invested in clean energy in the UK in 2015, compared with £11bn invested in UK oil and gas, according to Oil and Gas UK's *Economic Report 2015*. Major projects included the 580MW Race Bank and 336MW Galloper offshore wind farms, with estimated costs of \$2.3bn (£1.6bn) and \$2.9bn (£2bn) each.

iStock





The figures for 2016 are likely to be lower though, following the Government's decision in December 2015 to cut £500m–£600m of support, including lower feed-in tariffs for solar, wind and hydro power. But the renewables sector has proven adaptable in the past and has the ability to cope this time too.

“Every time there's been a cut in subsidies, the initial response of the industry has always been that it's the end of the world; there won't be any more investment,” says David Goatman, head of energy at consultancy Knight Frank. “And they pretty much always find a way to continue to develop projects.”

While the industry may suffer a short-term dip, the long-term need for renewable energy will not disappear. Under EU law, the UK is obliged to source 15% of its energy from renewable sources by 2020, including 30% of its electricity, 12% of its heat and 10% of its transport fuel. That requirement may fall away post-Brexit, but there are other targets in UK domestic law that will still apply, including the Climate Change Act 2008, which requires the UK to reduce greenhouse gas emissions by 80% by 2050.

PLAYING CATCH-UP

At the moment, the UK is still a long way behind some European countries. In 2015, 22.4% of the UK's electricity came from renewable sources, according to BEIS. In comparison, Denmark

sourced 58% from renewables, followed by Sweden (57%) and Italy (42%).

Even so, renewable energy in the UK has seen strong growth in recent years. Electricity generated from renewable sources grew 59% between 2011 and 2015, from 34,529 gigawatt hours (GWh) to 83,550GWh. That compares with a 43% increase during the preceding four-year period, from 2007 to 2011.

22.4% of UK energy came from renewable sources in 2015

SOURCE: OFFICE FOR NATIONAL STATISTICS

To put these figures into perspective, the average household in England and Wales consumes 16.1 megawatt hours (MWh) a year, according to the Office for National Statistics. This means that in 2015 the renewable sector theoretically covered the needs of around 5.2 million of the country's 24.4 million households. In comparison, household coverage in 2007 was 1.2 million and 2.1 million in 2011.

So the bigger question is not so much whether there will be investment, but where the investment might go. A 2015 report by consultancy firm PwC, *State of the renewable industry*, estimates that £40bn has been spent by the UK in pursuit of its EU renewable

energy targets since 2010, and a further £48bn is needed by 2020. According to its forecasts, annual investment levels will range from £5.8bn to £8.8bn in the second half of the decade, with offshore wind and solar photovoltaic projects taking the lion's share in electricity capacity.

NEW RESOURCES

The sources of investment capital have been expanding – in 2014, for example, the government-owned Green Investment Bank (GIB) and the Marubeni Corporation invested around £500m for a 50% stake in Dong Energy's 210MW Westernmost Rough offshore wind project in development off the Yorkshire coast. It was the first time GIB had taken on construction risk in offshore wind (it usually invests in operational assets).

It is not just about wind and solar though. According to the BEIS renewable energy planning database, there are more than 200 renewable energy projects under construction, involving 6.2GW of electricity-generating capacity. While many are solar and wind, they also include biomass, hydro and other energy sources. A further 700 projects with capacity of 22.5GW are awaiting construction.

There are plenty of options. Renewable energy is a broad term, covering wind, solar and hydro, as well as marine energy (wave and tidal), bioenergy (from burning plant or

SOLAR ENERGY

Solar energy offers many advantages. It can be deployed on a small scale, from individual applications like street lamps to houses and larger commercial deployments. Panels can be installed quickly and the energy source itself – solar radiation – is entirely free. So, it is perhaps unsurprising that solar power has become one of the main sources of renewable energy in the UK.

But there are some darker clouds on the horizon. A 2016 report from consultancy firm PwC, *Seeing through the gloom*, found that a third of jobs in the solar industry have been lost over the past year. The key issue has been the reduction of government support.

“Growth has slowed down,” acknowledges Reza Shaybani, chairman of the British Photovoltaic Association. “We always knew subsidies would be short-term but the Government let the industry down by ending the subsidies earlier than anticipated.”

He points out that costs have fallen sharply in recent years and dependency on subsidies is less than they once were. A report by consultancy firm KPMG for the Renewable Energy Association, called *UK solar beyond subsidy: the transition*, published in July 2015, points out that photovoltaic costs fell by 70% over the previous five years, and a further 35% fall is predicted by 2020.

The industry is already showing signs of resilience. Analysts say there has been a shift away from large ground-mounted solar projects, which had been the industry’s focus, to commercial industrial rooftop projects. Reza adds that British companies have also been looking more at export markets, a process which the BPVA started in 2015 and is already helping members to develop projects in some 22 countries.

animal matter), waste energy (such as landfill gas) and aerothermal, geothermal and hydrothermal energy (heat from air, ground and water respectively). Not all of these are low-carbon – particularly bioenergy. On the other hand, some other low-carbon sources, such as nuclear, are not renewable.

In the UK, the most important renewable source is wind, which provided almost half of all renewable power in 2015. Beyond that, plant biomass provided around a quarter, followed by solar photovoltaic (10.4%) and hydropower (8.6%). The smallest share came from marine energy, which provided 0.1% of electricity last year.

“Billions of pounds are being invested. It feels to me like the early days of solar”

One issue that has held back the renewable sector in the past has been its high cost compared to conventional sources. That remains a big issue for marine power, although some new schemes are being developed, such as the MeyGen tidal stream project in the Pentland Firth in Scotland.

However, the overall cost situation is now rapidly changing. The most recent figures from the Government – compiled in 2013 – show that the levelised cost (a measure used to compare different power sources) is falling for renewable energy but rising for conventional energy. The cost of onshore wind projects greater than 5MW, for example, is predicted to drop by 7% between 2014 and 2030 to £97/MWh. The figure for solar should fall by 43% to £90/MWh over the same period. In contrast, combined cycle gas turbine costs are expected to rise from £75/MWh to £88/MWh.

BRIGHT OUTLOOK?

The situation may actually be even better than that as, according to more recent research by BNEF, onshore wind is now fully competitive with gas and coal once carbon costs are taken into account. It says onshore wind projects had an average cost of \$85 per MWh (£67) in the second half of 2015, compared to \$115 (£90) per MWh for combined-cycle gas and coal-fired plants.

“Onshore wind and solar photovoltaic are both now much more competitive against the established generation technologies than would have seemed possible only five or ten years ago,” says Luke Mills, a BNEF analyst.

The industry has been used to receiving subsidies to help it close the price gap with conventional energy sources, but the Government’s decision to slash subsidies put it on the back foot, particularly for solar energy (see boxout). However, there is one area of the industry that appears to be booming and that is energy storage.

By its nature, renewable energy is more intermittent than conventional power – solar plants only work during the day, for example, while a gas turbine keeps working as long as fuel is supplied to it.

Developing storage for renewable energy addresses this problem and is attracting considerable interest. “Billions of pounds will be invested,” says David. “Storage is where most of the new money is going. It feels to me like the early days of solar.”

To date, the main storage solution has been batteries. Household names such as Siemens, GE and Tesla have all been involved in development. But some newer technologies are also beginning to emerge.

For example, the UK’s redT energy storage has recently installed its first ‘flow machine’ on the Isle of Gigha in Scotland, which stores energy in liquid form, rather than in conventional batteries.

CHALLENGES IN STORE

The improvement in storage technology could encourage the development of more localised/microgeneration renewable energy deployments, particularly for sites far removed from the National Grid. However, the degree to which this will take off depends to some extent on the level of feed-in tariffs offered by the Government.

Scott McGregor, CEO of redT energy, says the UK is still behind the leading markets when it comes to storage, although he predicts it will accelerate in time. “I am quite pessimistic right now in the UK as a viable market for energy storage. Energy storage comes down to economics. You’ve got to make money,” he says, pointing to parts of Africa and Asia as well as Germany, the US and Australia as more attractive. “The UK is definitely behind the other markets, but it will hit a tipping point and it will suddenly take off.”

It could almost serve as a model for the UK’s renewable energy as a whole: there is plenty of potential still to come and, while the short term may be tricky, in the longer term the industry should thrive.

The generation game

HOW DO FINANCIAL PLANNERS FROM DIFFERENT GENERATIONS APPROACH THEIR WORK? WE SPEAK TO JOHN, 26, AND MICHAEL, 78, BOTH FROM BHP WEALTH

◆ GARETH FRANCIS



Getty

With more people working longer and retiring later, many industries are facing new challenges that come with a multigenerational workforce.

The situation is no different in financial planning, where pre-war Traditionalists (born pre-1945), post-war Baby boomers (born 1945 to 1964), Generation X (born 1965 to 1976), the Millennials (born 1977 to 1995) and the young men and women of Generation Z (born 1996 onwards) are now working side by side. But do different generations within the industry have different skills and abilities? Do they hold different values? Or is age simply a number?

John Redmond, a financial adviser at BHP Wealth, is 26 years old. The firm's founder, Michael Freedman, is 78 years old. The two, who work closely together, discussed their experience as a cross-generational team.

WORKING TOGETHER

John and Michael handle around 100 accounts together. However, each will normally take a lead on different projects, depending on who is most appropriate for the

client in question. For example, Michael will often work more closely with older clients who are reaching the later stages of the financial planning cycle, especially those he has advised for a long period. John will often deal with the children or grandchildren of these clients. He explains: "Those clients will need a financial planner for many more years than their parents so it stands to reason that the younger adviser will begin cultivating those relationships."

Michael agrees: "It gives the younger client greater confidence that the person they are dealing with most is going to be around for as long as they need them."

"We're giving that same level of service and following that same process"

Other accounts require them to work more closely together, such as clients who are likely to continue needing financial advice after Michael retires. In these cases, the two will use their individual skillsets to assist them.

John notes they have naturally divided up the requirements of these clients accordingly, and that due to the way they deal with them, clients will know who to go to for what. He explains: "99% of our clients have a cashflow model which we maintain for them. Our clients know this is an area I now handle and to direct questions around it to me. If they are looking for a spot of advice or an opinion on certain things, perhaps a will, they would be likely to contact Michael. But clients tend to know who to contact due to the relationship we have with them."

However, this split between accounts handled individually and those worked on together can lead to certain challenges, such as the management of workloads, John adds. "The way we have naturally grown to work together is that Michael is the relationship manager on the names we work with together, but the preparation, follow up and day-to-day requirements are the areas I look after. When I joined Michael I was a paraplanner. I'm still fulfilling that role for those clients and advising where appropriate. But because I often have a long list of things

to do, while much of Michael’s role is fulfilled in the two-hour meetings, we have to avoid diary conflicts.”

SETTING STANDARDS

One area where their approach doesn’t differ is the six steps of financial planning, which, Michael notes, all advisers adhere to as a principle of good practice. He explains: “The process is such that it can be carried out by anybody of any age with the right qualifications. The qualification is key and I wouldn’t respect John as much as I do if he hadn’t knuckled down to be fully qualified. The steps aren’t handled any differently by either of us and that’s laid down in our processes.”

John agrees: “We’re giving that same level of service and following that same process for all clients. All our advisers are doing that and it doesn’t change between generations. It doesn’t matter what age you are or what stage in your career you’re at. Ultimately, all your clients should have that full six-step process if we are doing our job as financial planners.”

John adds that the two also work at a similar pace, and that while the desire for quick decision-making is sometimes considered a trait of younger generations, in financial planning that speed is set by the requirements of each individual project. “If a job comes along that needs doing, we both want it done as soon as possible,” he says.

DIGITAL DIFFERENCES

Perhaps unsurprisingly, the two do take different approaches when it comes to technology. John explains: “Michael can be a

technophobe! However, our roles mean I will be the one to do analysis for clients nine times out of ten. So for example, if it comes to analysing their investments or building their cashflow, I’m very familiar with the software. Michael on the other hand is less familiar with it.”

While Michael may not be as adept with certain technologies as John, he has long been an advocate of their implementation. “I ran a manufacturing company from 1960 to 1984,” he says. “Between 1969 and 1970, we installed a mainframe computer that filled a room and required a whole host of punch card operators to work. Technology now has superseded that and we can do most of that now with a tablet or smartphone. Anyone we employ is technologically literate but I feel I don’t need to be now.”

The two also hold different views on meetings, but are in agreement that an appropriate level of formality should be kept. “Both of us are fond of maintaining a regime of face-to-face meetings with clients,” says John. “I would like to be able to take some of our meetings with clients online but there are practical implications that stand in the way of that.”

FOUNDATION OF RESPECT

Michael and John believe that the key to a positive working relationship, regardless of age, is to recognise each other’s strengths and respect the different ways of working.

“I’ve learned an awful lot from Michael, such as the optimal way to deal with clients and how to deal with sensitive situations,” says John. “On the other hand, if he needs to deal with an issue around pensions protection and the many regimes that have been introduced over the past ten years, that’s something I can help him with. I think it works pretty well.”

Michael concludes that his early experiences in his own career still affect his approach now, and that this is why a good balance has been achieved between him and John. “My father was the founder of a manufacturing company and there was a terrible intergenerational gap between us. I was a qualified chartered accountant; he was a self-taught business person. He was far more intelligent than me, but he didn’t have the technical knowledge I had. He would turn down my suggestions because he thought he knew better than I did because he’d learned it all before I was even born. My years of strife working with that gap led me to choose not to persist with it. I’d rather treat people as equals.”

AGE MYTHS BUSTED

While many stereotypes exist about the strengths and weaknesses of different age groups, it seems that the perceived challenges of a multigenerational workforce are not noted by either employers or employees.

As indicated by both John and Michael in this article, most see working with colleagues of different ages as a benefit.

The Chartered Institute of Personnel and Development’s 2014 study, *Managing an age-diverse workforce: employer and employee views*, finds that when asked to rank the challenges of an age-diverse workforce, the most popular answer from employers is that there are none. For employees, the same answer is the second most popular, just below a lack of shared interests.

The same survey finds that knowledge sharing is seen as a key benefit by both groups.

Challenges of an age-diverse workforce according to employers

- No particular challenges 17%
- Age stereotyping 16%
- Internal progression/succession planning problems 16%

Challenges of an age-diverse workforce according to employees

- Lack of shared interests 32%
- No particular challenges 31%
- Misunderstandings 29%

Benefits of an age-diverse workforce according to employers

- Knowledge sharing 55%
- Enhanced customer services 14%
- Improved problem solving 9%

Benefits of an age-diverse workforce according to employees

- Having different perspectives 72%
- Knowledge sharing 66%
- New ideas 41%

THE SIX STEPS OF FINANCIAL PLANNING

1. Establish and define the relationship with the client.
2. Collect the client’s information.
3. Analyse and assess the client’s financial status.
4. Develop the financial planning recommendations and present them to the client.
5. Implement the client’s financial planning recommendations.
6. Review the client’s situation.

Source: Financial Planning Standards Board

◆ NICK MARTINDALE

Fresh meet

Over the past few years, there has been a steady shift towards the use of digital meetings, whether through videoconferencing or web-sharing platforms designed to allow people to share documents and information on-screen while chatting. Research by enterprise communications research firm No Jitter suggests that 87% of people use videoconferencing more today than they did two years ago, but this is a trend that has been developing over the past two decades.

Electronic meetings were first developed in the 1980s, out of university and research projects, and then started to be used in earnest in businesses in the 1990s, running over local area networks. But it was the development of browser-based systems in the 2000s that really saw the technology emerge as a viable alternative to meeting face-to-face.

It was a trend that picked up pace during the economic downturn as organisations looked to reduce travel costs, and has been further boosted by improvements in technology and broadband provision over the past few years. According to research by consultation firm Frost & Sullivan into the European

conferences services market, the industry was worth \$1.78bn in 2013, and is expected to hit \$2.58bn by 2019, across audio, hosted web, hosted video and managed videoconferencing services. Around half of this is expected to be made up of audio conferences – down from 61% in 2013 – with web conferencing forecast to account for a quarter of the market by 2019.

Like others, the financial planning sector is starting to take advantage of this, using such meetings as a means of discussing arrangements with clients without the need to bring them into the office or meet in person.

MAKING THE MOST

Rob Noble-Warren CFP™ Chartered FCSI, CEO of private client asset management firm Independence Wealth Management, actively encourages digital meetings with clients, although the business usually insists on an initial face-to-face meeting. “You do need a personal connection,” he says. “All the research says you don’t have a good relationship unless you meet the person. That’s required, but it’s only required once or twice, not on an ongoing basis.” He uses a combination of telephone and web-sharing software Yuuguu,

but resists Skype, he says, because “the 2% of the time when it doesn’t work properly can be really annoying.”

Andy Jervis CFP™ Chartered MCSI, director of Chesterton House Financial Planning, also deploys the technology, in particular GoToMeeting and GoToWebinar, and is increasingly finding that clients are requesting this as an alternative to meeting up in person. “It can be more efficient, partly because people tend not to talk so much and not to be so expansive on the phone or online,” he says. “When someone comes into our office they often want to sit down and have a cup of coffee and a chat, and when you’re on the phone in your front room or office, meetings tend to be shorter. But our business is very much about the relationship as well, so meetings are not just focused on financial issues.”

Joanna Hague CFP™ Chartered MCSI, a paraplanner at Investment for Life, says that her firm regularly uses Join.me, which can come in handy when clients need conversations in a short timeframe. “Our use of this has increased over the past six months to a year, because we’ve been suggesting it to



Getty

clients,” she says. “We explain that we can meet in a couple of weeks or, if they like and they’re in front of a computer, we can look at it now. It’s particularly useful when we’re doing cashflow planning, because they can see what it would do to their financial position if they gave some money away to their daughter, for example.”

The business also uses it to improve its own efficiency. Joanna often ‘attends’ meetings online that are being held in person between an adviser and client. “I join their meeting online from my desk, as a paraplanner,” she says. “It means I can listen and join in, but it also allows me to write the minutes while the adviser is talking to the client, and before he gets back to the office they’re ready to be signed off. The work is done while he’s travelling back, and I don’t have to rely on the financial planner bringing me back a set of notes.”

A QUESTION OF SUITABILITY

Brett Davidson, founder of financial planning consultancy FP Advance, says that, while some planners are using this technology, the sector has yet to fully embrace its potential. “I’ve definitely heard of examples of it but my sense is that it’s not used that much, and even a firm that’s open to it might only do it occasionally,” he says. “Very few have really promoted it positively.”

However, those that have deployed digital meetings have had positive experiences, he adds, and it can be more convenient for all parties. “There’s obviously going to be demand from clients travelling or living abroad, but in every town I go to in the UK the traffic seems to be an absolute nightmare, so why make people travel an hour each way and get caught up in the after-school traffic? It’s attractive even for people who live locally.”

He’s also used this technology himself in his capacity as a non-executive director of a number of other businesses, he says, helping to reduce the need for face-to-face meetings. “We tend to meet quarterly and I’ll go to their office, but in between that every month we have a check-in call, which we do over the phone or via Skype,” he says. “It’s becoming a bigger part of what we do.”

The suitability is dependent on circumstance, says Andy. For example, he usually insists on a face-to-face meeting when first meeting a client. “There are three reasons why we normally insist people come to our offices if we’re meeting them for the first time,” he says. “First, meetings can go on for quite a long time and on an internet connection that

can be quite difficult; second, you can build a relationship more effectively face-to-face.

“But the most important reason is that it shows a commitment on the part of the clients to actually enter into this arrangement. It shows that they are prepared to take their own planning seriously and make the time commitment it deserves.” It also depends on what services they are interested in, he adds. Financial life coaching tends to require more in-depth discussions that would be more difficult to do virtually.

“When you’re on the phone in your front room or office, meetings tend to be shorter”

Brett, however, believes businesses that fail to offer digital meetings as an option for clients could be in danger of not putting their customers first. “I would be proactively telling my clients that digital meetings are available to them, if they want them,” he says. “If your business is all about customer service, I can’t understand why you wouldn’t at least get some feedback from your clients on what they want.”

In the longer term, Andy believes that the use of digital meetings should help planners not only keep clients who have moved out of a local area, but even potentially gain new ones. “If you have a practice which has a good reputation, you can attract clients who are not in your normal catchment area,” he says. “For example, we’re based in Loughborough in Leicestershire and I’ve just been working on a financial plan for clients who live in Bradford who were recommended by someone who lives locally. They’re quite happy to make the trip but it’s still a long way down and we wouldn’t necessarily expect them to do that every time.”

The deployment of such technology is only likely to become more common, adds Andy. “As the technology and the quality improves it will become easier. My own view is that within a few years you’ll almost be talking to a hologram sitting in the corner of the room.”

This is not quite as futuristic as it seems. The use of virtual reality means that people from all over the world could take part in meetings as holograms where it appears that they are all in the same room, using devices such as the HoloLens. This, in turn, could change how organisations use such technology; a recent study conducted by PGI, for instance,

suggests that 66% of job candidates now prefer video interviews over travelling to meet a potential employer.

Joanna, however, sounds a word of caution about just how far the use of digital meetings should go. “We don’t want it to ever replace face-to-face meetings,” she says. “I think it has the potential to, but we have made a conscious decision that it shouldn’t, so if we meet for an annual review one year online, we wouldn’t do that again the next year. There is a risk you could abuse it, especially if you know meeting face-to-face is important to the client. You have to judge each situation; we certainly aren’t forcing them on people who don’t want to do it.”

WHICH PLATFORM IS RIGHT FOR YOU?

There are a number of platforms available to organisations looking to make use of digital meetings, and which one is most appropriate will depend on both need and budget (most will offer a free trial if you’re unsure). These can be roughly divided into three categories.

Full systems: With prices for full systems starting at around £35 a month for up to 100 users, these offer the most comprehensive features and can often be customised to customers’ individual requirements. Examples include Adobe Connect; Citrix GoToMeeting; Skype for Business and Cisco WebEx.

Basic systems: With prices starting from £30 per month for multiple users or £5.75 for single users, these are designed more for those who require only limited functionality, perhaps for fewer users or less frequent use. Examples include Yuuguu, Join.me and MeetingBurner.

Free systems: These are designed to let organisations test out the functionality, with the option to pay for more sophisticated features, as well as support from the supplier. The main examples are Google Hangouts and Skype.



iStock

A big impact

IMPACT INVESTING HAS EVOLVED, WITH A RANGE OF NEW FINANCIAL MODELS EMERGING TO HELP INVESTORS MAKE A DIFFERENCE. WHAT LIES AHEAD FOR THE INDUSTRY?

◆ JILL INSLEY

All investors want their money to work hard, but impact investors are possibly the most demanding of all: they not only want their money to produce a financial return, but a positive social and environmental benefit too.

There is a difference, however, between impact investing and traditional ethical or socially responsible investing, where investments are made according to a firm's environmental, social and governance (ESG) criteria. ESG investments filter out

the companies that don't meet certain criteria, and impact investing looks at companies that have a specific goal of improving society through their actions.

Global International Financial Reporting Standards Leader and UK Head of Accounting and Corporate Reporting at Deloitte, Veronica Poole, says the two should not be confused. "Traditional ESG investing is focused on screening out the negative. For example, a fund manager might look at a company's energy

use, waste or pollution and decide not to invest if the company is having a negative impact on the community or environment around it."

By contrast, impact investing analyses the ESG factors of a company, but also looks at how that company can generate a positive impact and a profit. "Impact investing looks for both the beneficial social or environmental effect that a company can have alongside a positive financial return," adds Veronica.

Investors range from specialists like Impetus-PEF, a charity that emerged from a merger between the Impetus Trust and the Private Equity Foundation, and Big Issue Invest, the social investment arm of the eponymous magazine.

There are also foundations, wealthy families and individuals involved in this space. The increasing diversity of investment structures and beneficiaries means that a growing number of investors can satisfy their social and environmental interests alongside their financial goals.

FUNDING METHODS

Impact investments can take a variety of forms, from loans and guarantees to private equity funds, with the type used depending on the needs and structure of the beneficiary. One of the most prominent forms of investment is social impact bonds (SIBs), which is an area where the UK industry has led the way.

SIBs are contracts with the public sector in which a commitment is made to pay for improved social outcomes that result in public sector savings. According to the UK Government, investors pay for the project at the outset, and then receive payments based on the results achieved by the project.

The bonds are designed to attract private investors to fund early and preventative action for complex and expensive social problems.

Investors can satisfy their social interests alongside their financial goals

The first SIB, launched in 2010, was designed to reduce reoffending among short-term male prisoners in Peterborough prison. Seventeen foundations committed £5m to fund rehabilitative interventions for male offenders sentenced to less than 12 months in prison. The Ministry of Justice, supported by the Big Lottery Fund, agreed to pay a return to investors if targets for reducing reconvictions were achieved.

More than 60 SIBs have now been established, with 31 active programmes in the UK, and the first are beginning to mature. The first group of prisoners included in the Peterborough SIB needed to achieve a 10% reduction in reoffending compared with a national control group to trigger an early payout to investors, but missed this target by 1.6 percentage points. The second round of results is likely to be released early in 2017.

However, others have proven successful. A SIB set up in 2012 by the Department for Work and Pensions (DWP), supported by Impetus-PEF and Big Society Capital, to provide funding for a project run by London-based charity ThinkForward, completed successfully in October 2015.

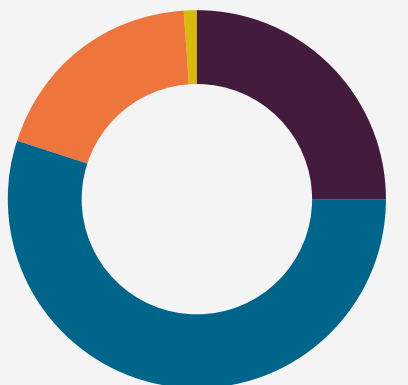
The project, which received funding of £900,000 by the SIB, paid for ‘progression coaches’ to be placed in 14 schools in Tower Hamlets, Islington and Hackney. It provided five years of one-on-one intensive support to more than 1,000 disengaged young people from the age of 13.

To trigger payout to the investors, the project had to meet a series of outcomes, including improved attendance and behaviour at school, level 1, 2 and 3 qualifications, entry to university and employment and sustained employment.

Programme Development Manager for ThinkForward Luke McCarthy says: “We were lucky that our investors were genuinely committed to the social outcomes. This meant that we were able to stick to our core mission of supporting young people furthest from employment, who understandably needed more intensive support, and also not simply ‘park’

SOCIAL IMPACT QUESTIONS

When choosing an investment, how important are financial returns in your decision-making process?



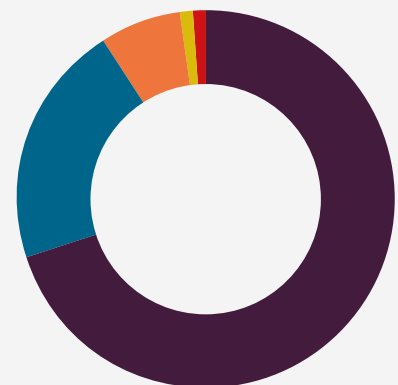
- Financial returns are the only factor I consider when choosing where to invest
- Financial returns are the most important factor but I consider other factors when choosing where to invest
- I consider financial returns but they are not the most important factor when choosing where to invest
- Other
- I do not require a wealth manager as I am an execution only investor

When selecting a wealth manager, would their knowledge of social/environmental impact and/or return influence your decision to choose them?



- Yes
- No
- I do not require a wealth manager as I am an execution only investor

Please indicate the extent to which you think your primary wealth management provider should make improvements in the following non-investment related areas



- No improvement needed
- A little improvement needed
- Significant improvement needed
- Very significant improvement needed
- Other

Source: ComPeer survey of 1,005 wealth management investors and clients, November 2014

young people in a job which was not right for them in the long term, but which generated an outcome payment for the SIB.”

Bridges Ventures, a specialist impact investor, has become one of the biggest participants in the UK SIB market, supporting 13 contracts to date. These early SIB investments were made from the Bridges Social Entrepreneurs Fund, a £12m closed-ended fund launched in 2009 to invest in social enterprises and charities delivering clear social impact. This fund recently won the Investing and Financing prize at the 2016 Finance for the Future awards, which is a collaboration between the Institute of Chartered Accountants in England and Wales, The Prince’s Accounting for Sustainability Project (A4S) and Deloitte. One of the reasons for its victory was its development of a new form of quasi-equity, whereby the investor is repaid if the borrower succeeds in meeting various growth and impact targets. This was designed as a way of providing growth capital to ambitious charities that have difficulty raising equity investment because of the way they are structured.

Lack of liquidity may also be a concern for investors interested in the sector

One of the fund’s notable successes has been Care and Share Associates (CASA), an employee-owned social enterprise providing domiciliary, health and social care to the elderly, disabled and vulnerable. In 2011, the fund invested £400,000 in CASA, enabling it to provide about 4,500 hours of care a week. Four years later, CASA was supplying more than 16,000 hours of care a week, employing more than 700 people, 93% of whom were drawn from under-served areas. CASA’s success enabled it to raise a second round of social investment, led by Big Issue Invest – which repaid the Bridges loan in the process.

Bridges Ventures is now raising a successor vehicle to its first fund, with the aim of being able to provide financing and support to mission-led organisations like CASA over a longer timeframe.

THE FUTURE

So how does the impact investment sector go about growing? Until now attention has been focused on high-net-worth, corporate and institutional investors, but now the

sector is beginning to consider expanding to retail investors.

In France, a ‘Solidarity Investment Fund’ has more than one million investors and assets of more than €6bn: 10% of the fund is invested in social organisations dealing with issues such as housing, employment and the environment. Here in the UK, the innovation charity Nesta has called for the launch of an ISA specialising in impact investing, while the Social Market Foundation and Big Society Capital – the funding ‘wholesaler’ underpinning this sector – have called for the Government to encourage savers to invest in a new type of social pension fund.

But the first challenge, however, is to help investors understand the different kinds of impact investment – and the different investment products available to them, depending on their impact preferences, liquidity needs and risk/return appetite.

Head of Communications at Bridges Ventures, James Taylor, says that one key constraint on the growth of the market is the lack of a standard convention for investors to talk about the kind of impact they want to achieve and what success might look like – which is essential if they are to construct a portfolio and measure their impact in a meaningful way. To this end, Bridges Ventures is spearheading a new global initiative of industry participants to develop a standardised way for investors to talk about and manage against their impact goals – just as investors have for their financial goals.

IMPROVING LIQUIDITY

Lack of liquidity may also be a concern for some investors who are interested in the impact investment sector. The Social Stock Exchange (SSX) solves this problem in two ways. First, all SSX members are screened by an admissions panel to ensure they have a pro-social or pro-environmental mission at their core, and must submit an impact report on an annual basis. About half the members are listed on exchanges such as the London Stock Exchange and Euronext, which means investors can use their membership of the SSX to validate a company’s impact ‘credentials’ before using their regular retail stockbroker to buy their shares. Second, the SSX offers its members the option to list equity on the SSX segment of the ICAP Securities and Derivatives Exchange

(ISDX). The SSX helped businesses raise more than £400m in 2015 alone.

Chief Executive of the SSX, Tomás Carruthers, says: “Historically, impact investments have been the preserve of high-net-worth investors, private equity and family offices, as there is typically no secondary market for the investments. The SSX can provide this secondary market, so a retail investor can get involved, confident that if they need access to the capital, this can be achieved.”

“We have to get this right for the charities and social enterprises receiving capital”

Barclays conducted research last year finding that while 56% of a sample of 1,800 retail and high-net-worth investors were interested in impact investing, only 9% had followed through on the idea. Head of Impact Investing at Barclays, Damian Payiatakis, says the research also showed that many people are confused by the investment options and terminology, such as the difference between ESG and impact investing.

Likewise, respondents to the FCA’s 2015 *Call for input: regulatory barriers to social investments* reported a low level of awareness of impact investing in the adviser community, with many not understanding the difference between social enterprises and other forms of business, or the importance of promoting an enterprise’s social impact. Barclays intends to do further research in 2017 to refine the development of a profiling tool to help investors and their advisers identify their interests and preferences, integrating impact investing into the normal investment process. The FCA has decided to maintain its current regulatory requirements for the social investment sector, including the suitability test, as this “protects individuals who are risking their money, but may not have an understanding of the market in which the business will operate and the chances of its success”.

Damian agrees with this stance: “This is a nascent industry. We have to be cautious and get this right – that is vital both for the charities and social enterprises receiving capital and the investors who are providing their money. When we do, investors can both protect and grow their assets and make a positive contribution to the world.”

CHANGE: REGULATORY UPDATE

We live in strange unsettled political times and this is disturbing financial regulation. Firms on both sides of the Atlantic are required to prepare for planned new rules while being told to make contingency plans for the unexpected, whether those relate to new US presidential policies or Brexit. The articles below start with looking into this, before returning to the normal approach of firms' present concerns.



Christopher Bond, Chartered MCSI, *Change* editor



Christopher Bond, Chartered MCSI is a senior adviser to the CISI. He has extensive experience in financial regulation, both as a lawyer and as editor of the CISI's well-regarded regulatory magazine, *Change*, which he edited for ten years. He gives presentations on many EU and UK regulatory subjects in the UK and Europe, and writes for a number of regulatory publications. He also supports the CISI's Compliance and European Regulation Forums and advises on *Professional Refresher* modules. He is a bank board director and editor of *The International Banker*, the magazine of the Worshipful Company of International Bankers.

Top regulatory developments

1. The Trump effect on financial regulation

This affects US-based firms directly, but indirectly applies to all firms, even UK domestic ones. The President-elect has said he wants to reduce regulation and roll back much if not all of the Dodd-Frank post-world crisis reforms. These most affected limiting proprietary dealing by banks, but there has been less comment on the effect on other financial sectors, such as swaps execution facilities for derivatives and prudential requirements for firms. The President or Treasury Secretary may find it difficult to delay or reverse these changes made by government agencies, such as the Commodity Futures Trading Commission. So US firms must continue to implement Dodd-Frank while perhaps hoping that their preparation may be wasted. Non-US firms with US offices, clients or counterparties should not expect greater access to the US – rather the reverse if the US no longer follows the G20 Pittsburg commitments and becomes less equivalent. Firms seem to be analysing the new President's and his advisers' statements intently and waiting to learn more of the new Administration's policies before taking action.

2. What should firms do about Brexit?

The argument continues of what the negotiating approach of the UK should be in Brexit negotiations, and of the importance of the City's contribution to the UK economy and of its need for EU nationals. And for a transitional period after the Article 50 notice expires. Here is my analysis of what firms are currently planning or doing:

- Those with EU business and continental affiliates with relevant licences can most easily shift the business and staff to EU affiliates.
- Third country firms with EMEA (Europe, the Middle East and Africa) head offices in the UK may move the whole to the EU or just the EU part.
- UK firms with little EU business may simply stop having clients based in the EU (including UK expats) or have an EU intermediary.
- Other UK firms with some EU clients or counterparties or exchange or clearing house memberships face a dilemma – should they set up an EU presence or possibly abandon this? Is the cost of establishing one and the capital required to do so more than its value? And if so, can the EU presence have back-to-back arrangements with a UK firm so only part of the front office moves out of the UK?
- EU firms with UK business face the access problem to UK wholesale and retail clients equally.

Given the time needed to obtain licences and move operations to another country, measured against the two year notice period under Article 50, many of the most affected firms have decided to start their contingency plans in early 2017. It seems unlikely any agreement on future arrangements can be reached before then. Frankfurt, Amsterdam and Paris may not gain what London loses – third country firms may simply repatriate the offshore functions to non-EU head offices.

All firms should have a plan. Andrew Bailey, CEO of the FCA, recently said to the Treasury Select Committee: "They [firms] should have a contingency plan because we ask them to have a contingency plan for every other scenario and event that could pose a risk for them, so it would be inconsistent not to have one here."

3. 'Hot spots' under MiFID II

The FCA has made it plain that UK firms should continue to prepare for the start of MiFID II in January 2018, despite the official delay of at least one part, eg, market shares of multilateral trading facilities (MTFs) since the European Securities and Markets Authority (ESMA) will not have the data, and rumours of further delays. For firms the clinching point is the need for the UK to be equivalent if it is to have the opportunity of EU access. The September FCA Consultation (CP16/29)¹ on implementing key elements of conduct of business, such as unbundling of research and transaction charges, costs disclosure, product governance, firms' independence and best execution is a good source; as is the ESMA guidance² including the latest on transaction reporting, reference data and order record-keeping. Here are a few of the hot spots for firms:

- Whether the firm is a 'systematic internaliser' (a firm which, on an organised, frequent, systematic and substantial basis, deals on own account by executing client orders outside a regulated market, MTF or organised trading facility). This matters because of the market making, best execution and reporting obligations that go with that status. Some argue that over-the-counter transactions under the rules of a regulated market escape.
- The refusal of the FCA to give detailed guidance on how firms should disclose costs throughout the value chain to clients, so firms must decide with the help of trade bodies.
- The definition of 'clients' under MiFID II to include professional as well as retail clients with unexpected consequences, eg, in disclosing inducements and conflicts of interest.
- The new duty on product distributors (including execution-only customers) to tell providers who the end customer is so the provider can check that the investor is in the target sector for the product – even though the distributor has not collected the data or fears that the provider will cut it out if the provider also sells direct (much data demanded, little data agreed to be provided by distributors).

4. ESMA knowledge and competence guidelines

The European Securities and Markets Authority (ESMA) guidelines, issued under MiFID II, mandate national regulators to require individual advisers to have sufficient knowledge through qualifications and experience to be competent to advise retail and professional clients on a wide range of investments, and to keep their knowledge up to date through continuing professional development. It extends this to a new category of information providers who do not provide advice, eg, bank branch or call-centre staff who select the appropriate information on investments for potential investors.

In the UK the Retail Distribution Review (RDR) already requires retail advisers to have a qualification; however these are limited to 'retail investment products', which excludes such investments as stocks and bonds, rather than funds investing in them. The RDR is also limited to retail clients, unlike the ESMA guidelines – which also set out the core standards to be included in the qualifications. The FCA has issued its consultation (CP16/29) on how it plans to implement this.

Firms will need to consider whether they have staff who will need to become qualified now, given that there is only a year before the requirement starts, and there is no 'grandfathering' provision for existing staff (although unqualified staff can continue to work under supervision for five years until they pass the exam). The CISI is reviewing its qualifications to ensure it has these for both advisers and information providers.

5. FCA strategy review

The CEO of the FCA, Andrew Bailey, has launched a strategic review. He wants comments from all parties on what its mission should be – although it already has strategic objectives under the Financial Services and Markets Act, such as clean markets, investor protection and competition – so it wants to know more about how to achieve these. This will inform the focus on better and clearer regulation – making clear externally and internally what the realistic expectations of firms, consumers and politicians are. Some pointers to his new policy are in his criticism of the size of the Handbook (over six feet high if printed out) and clearer policy and supervisory thinking – looking at what is important rather than box ticking; maybe having more trust in firms and being more selective in punishing them; protecting those vulnerable consumers who need it most; and being prepared to interpret its mandate more widely, eg, in commercial lending.

This is the first deep review of the FCA since its formation under its first CEO, Martin Wheatley. Firms and consumers alike are asked to contribute their comments before January with their 'wish' lists.



1. <https://www.fca.org.uk/sites/default/files/cp16-29.pdf>

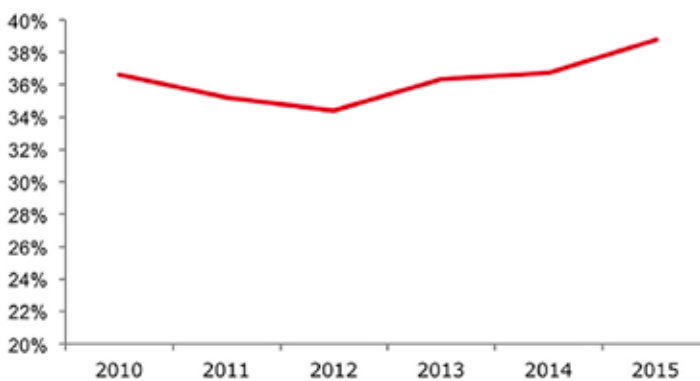
2. https://www.esma.europa.eu/sites/default/files/library/2016-1452_guidelines_mifid_ii_transaction_reporting.pdf

6. The FCA's interim asset management report

This long-anticipated market study³ into retail and institutional asset management has made some strong proposals for change. However, the FCA has stopped short of capping management fees as some had feared. It found that there was weak price competition among active fund managers; that the typical 36% managers' operating profit margin was too high; and that this resulted in a typical active fund delivering 25% less before transaction charges (and about 45% less after these) than a typical passive fund, over a 20 year period. The most interesting changes proposed are:

- a stronger duty on managers to obtain value for money in the value chain, eg, in best execution and forex charges
- requiring an all-in figure and clearer communication of fund charges and their impact at the point of sale
- requiring increased transparency and standardisation of costs and charges information for institutional investors
- requiring greater and clearer disclosure of fiduciary management fees and performance.

Average operating profit margin for active fund managers



Source: FCA analysis based on financial data submitted to the FCA from 16 firms

7. FCA platform and financial advisers review

In the asset management report the FCA also sets out its agenda to enquire into whether financial advisers and platforms provide clients with value for money. "Platform best buy lists, third party ratings and potentially financial advisers may influence how retail investors allocate their assets." It went on to give examples of areas for investigation. "Approximately 78% of retail investment fund sales in 2015 were advised." These include best buy lists, third party ratings, financial advisers failing to give prominence to passive funds, adviser networks promoting in-house fund of funds and model portfolios narrowing asset manager choice. Whether platforms deliver value for money will also be scrutinised because 80% of new retail investment sales were executed through platforms in 2015. "Retail investors do not appear to benefit from economies of scale by pooling their money together through direct to consumer platforms."

If the consultation proposal is confirmed, firms should expect the FCA to take the same approach to its asset management

investigation such as round tables, questionnaires and thematic visits. The background is recent research that suggests the RDR has only made a small reduction in typical fees charged to retail clients.

8. FCA review of MAR implementation

Market Abuse Regulation (MAR) changes started in July 2016, and most firms were ready for it. However, industry-wide sticking points remain – most notably the requirement for firms to record orders that never became transactions. Many firms have struggled to collect this data in order to record it. They should be aware that the FCA is likely to make a thematic review of firms' implementation of the changes. On its past record the FCA may single out those it considers have not done enough for criticism – or even investigation. The sample of firms reviewed runs from small to large and across different sectors. Firms that consider MAR does not require them to make changes or that are still implementing it should be aware of this.

9. Extending the SMCR to all firms

The Treasury decided to extend the Senior Managers and Certification Regime (SMCR), increasing the responsibility of individuals to non-banks "during 2018". A consultation is planned in 2017, and FCA informal discussions with firms and trade bodies have already started. There are some important changes from the bank regime, such as keeping the normal responsibility of the FCA to show that a senior manager has failed in his or her area of responsibility to prevent a rule breach and not reporting breaches by individuals. However, the main parts of the regime will apply to all firms, such as senior managers having detailed statements of responsibility, and the individual conduct principles applying to virtually all staff, including treating customers fairly.

Since the regime will apply "proportionately", less complex firms may not be required to have an overall Responsibilities Map covering all required functions, or to take and give regulatory references, or for senior managers to give handover certificates to their successors.

As a first step, the FCA has sent a questionnaire to many firms to assess the SMCR's impact and to guide it in its implementation. Firms and senior individuals should start thinking now about how this radical regime will affect them, and how they should prepare for dividing up the required functions between managers, and to identify who will be certified staff – it took banks at least twelve months to do this.

10. The regulators' expectations on cyber crime

The recent raid on 20,000 Tesco Bank's customers' bank accounts has made firms' precautions against cyber crime an even higher priority – if that were possible. (The FCA has reported that the number of cyber attacks against financial services firms has soared in the past couple of years, with reported incidents to the City watchdog increasing by 1,500% since 2014.) Theft of data or denial of service is less direct than actual theft of money.

3. <https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf>

So now it is up to all types of financial firms to take action against all forms of cyber attack. This is both in terms of IT spend but also of staff awareness and training and having a tested communications plan if the worst happens. It is equally clear that the regulators on both sides of the Atlantic will punish a firm severely if it is successfully attacked, and the regulator considers the firm was either not prepared for it or ignored internal or external warnings of vulnerabilities or made an inadequate response to a successful attack.

11. The new foreign exchange global code

Much progress has been made in developing a global FX code which will not only apply internationally, but to both sell-side and buy-side, as importantly the approach to having a global set of principles of market conduct is likely to be replicated in other global capital markets. The co-operation between national regulators on acceptable and unacceptable market practices is a recent significant development, breaking down national regulators' prejudices. The fact that it is a voluntary code is unlikely to limit its effectiveness, given the high level support it has among powerful regulators.

The code will be rolled out in several steps – starting with the exercise of discretion, which should not disadvantage the client – taking pre-hedging as an example. The next step will address the use of the 'last look' and time stamping – both highlighted in the Fair and Effective Markets Review. It is structured with a general high level principle followed by the application of it to several points of concrete guidance.

The regulators expect firms to embed the code in their practices with training and education; establishing the right monitoring policies and procedures. Firms need to be able to demonstrate they are adhering to the code – the regulators favour public attestation for this. The Bank of England has said: "Individually, firms, and particularly senior management, should start considering the steps they will take to support the code."

12. More bank capital and liquidity requirements

We are at a critical point on these. Will countries support Basel in completing its programme to make banks safer after the financial crisis? There remain contentious decisions which could have a large impact on banks, such as harmonising the rules on banks and other firms' internal models used for calculating market and credit risk through a standardised capital floor and whether bonds issued by another bank should be included in a bank's prudential capital (total loss absorbing capacity), or not (here there are US/EU disagreements).

Relevant firms who are unhappy with Basel's proposals may hope that the incoming US Administration will take a softer line than currently but it may well be unwise to count on that happening.

13. The regulator encourages robo-advice

The financial industry continues to investigate and sometimes adopt robo-advice, with the regulator's encouragement. Many wholesale firms, exchanges and clearing houses are considering whether blockchain, with its multiple distributed ledgers, can speed settlements and reduce failure risks. Some retail asset managers and advisers are setting up robo-advice services, giving customers access to higher end products at lower cost alongside their human-led services. The regulator has given encouragement and special access to 18 firms, both large and small, existing and new, pioneering new robo-services to retail clients as part of its approach to filling the 'advice gap' identified by the Financial Advice Market Review and blockchain applications. Firms may consider whether they need to use fintech to develop new services.



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The rise of sustainable investing

In 2016 the investment world – notably including the UK and the US under its new President – began to focus on infrastructure, driven by a return of faith in fiscal policy and a demand for long-term income. The focus for 2017 could well be sustainable investing. Turn to page 44 for a masterful analysis of the issues surrounding sustainable investing, written by Quintin Rayer, Chartered FCSI, who brings his academic verve – he has a doctorate in physics from Oxford University – to bear on this complex but rewarding subject.

Sustainable investing has come of age during the course of this decade. The ‘Finance for the Future’ Awards, presented in Merchant Taylor’s Hall in October, are now in their fifth year. They are meant as a “celebration of leadership and innovation that creates sustainable businesses and economies”. This is no mere do-gooding piffle. The judges for this year’s awards included the chief financial officers of mainstream profit-oriented (and shareholder-responsible) businesses such as Adidas, Tesco and Wates Group.

Communication lies at the heart of this new approach to business. Veronica Poole, global IFRS leader and UK head of accounting at Deloitte – one of the sponsors of the programme – says: “What really stood out amongst the winners was authenticity and the way their integrated thinking shone through. Communicating in a way that truly explains what makes companies tick and the values they live by is extremely important in creating trust in business.”

The outright winner was the Coca-Cola Hellenic Bottling Company. The judges said the team there had “brought to life the vital role that the finance team can play to embed sustainability into everyday decision-making. It was able to develop an approach that systematically integrated environmental and social factors into capital expenditure across the diverse geographies, changing decisions as a result”. The winner of the award for ‘communicating integrated thinking’, Warrington-based United Utilities, was praised for “producing clear, concise, integrated communications [that] demonstrate how integrated thinking translates to shareholder value in financial terms”. That quality of communications, in an age when more clients are asking questions about the ethics and sustainability of their investments, needs work in the financial services industry – see Michael Williamson’s analysis of some of the issues, from Cass Business School, on page 43.

INVESTMENT VALUATIONS

The space value of money

A much-admired runner-up at the sustainability awards was Dr Armen Papazian. The *Financial Times’* Lucy Kellaway, presenting the awards, spoke for much of the audience when she remarked that while Dr

Papazian conveyed a fine sense of excitement about his theories, many in the audience, perhaps a little rusty in the mathematics department, would need to read his paper to gain the full benefit. We are delighted to give his paper its first public airing here in *The Review*. Dr Papazian’s model introduces a new principle of value, ‘Space Value of Money’, into our current risk-and time-based paradigm. He describes his model, equations and approach as ‘Space Time Finance’, and he is currently writing a book on the same, due to be published by Palgrave Macmillan in 2017. Dr Papazian, who has extensive financial industry experience, was previously a Fellow and Research Associate at the Judge Business School of Cambridge University, from which he holds a PhD in financial economics.

CORPORATE FINANCE

‘Cerf in the City’

CERF – the Cambridge Endowment for Research in Finance – runs this annual City event for practitioners, designed to stimulate discussion and research ideas that have practical relevance to the industry and to showcase some of the best and brightest research in finance that is done in Cambridge.



CAMBRIDGE
 Judge Business School

CERF promotes research in Cambridge University into all aspects of finance, financial institutions, and financial markets, and their relationship with economic behaviour and performance.

Professor Bart Lambrecht, Professor of Finance, Cambridge Judge Business School and a regular speaker at CISI events, is Director of CERF and Research Fellow of the CEPR.

Three fascinating talks from the latest ‘CERF in the City’ are now available to members on CISI TV: Dr Bang Dang Nguyen on ‘The impact of the external networks of directors on firms’, Dr Chryssi Giannitsarou on ‘Informative social interactions’ and Professor Raghu Rau on ‘Evangelical investors and evolution of local bias’.

DISRUPTION IN FINANCE

A needle in the #aystack

From bogleheads.org, to seekingalpha, to stocktwits, to the reddit investing forum, to quora, to twitter, it’s clear that a large proportion of today’s stock market traders are eager to share their stock picks online. The winning entry in a competition for masters students at the University of Edinburgh Business School, with which the CISI has a close working relationship, explores this exciting new field.

Social media information is a source of immense, if uncertain, value. Academic papers have proven that aggregate social media data can be used to predict the market. In the last five years, fintech initiatives and research firms have begun sifting through these volumes of big data to bring social media alerts to investors. Social media sentiment analysis is a bottom-up method to extract the feelings of investors about market securities from their online posts. It is now the bedrock of a rich environment of firms competing for the attention of funds and investors. This innovation has forced information services firms to innovate and react, and has contributed to the rise of alternative research providers. The technology is not without pitfalls, as it risks entrenching divisions between retail investors and nimble competitors, and magnifying deceptive practices.

A needle in the #aystack is a documentary made by Nic Carter, Aris Georgopoulos, Dennis Jacob, and Wenrong Lu. The team says: “Join us in an occasionally surrealistic journey into the world of social media trading insights.”

One of the two runners-up was a team of three students from Kazakhstan – Sagindyk Abildinov, Aida Kaliyeva and Aray Nugumarova – who produced a fascinating survey of blockchain in finance. It cleverly analyses some of the key challenges in this field, such as bubble behaviour and price volatility, illegal activities, the potential rise of alternative crypto currencies, different categories of altcoins plus numerous legal issues. But it also covers the many opportunities that blockchain technologies create, including lower transaction fees, open and decentralised networks, peer-to-peer networks with user control, opportunities for the underbanked and blockchain's pivotal role as a platform for future innovation.

Online trading, the other runner-up, is a documentary film about how the internet has disrupted and continues to disrupt the way we conduct trading. The film defines what online trading actually means and mentions some of the concepts that are parts of online trading. It analyses the historical background to understand how trading used to work prior to the internet, as well as how the internet revolutionised the way that people trade, which changed the face of the international financial market for good. The film also describes in detail the positive benefits of online trading for individual investors, brokerage firms, and banks. In addition, it considers the downsides and the future of the industry. This 25-minute film was produced by Wenqian Shen, Rami Elsirgany, Alfonso Pliego, and Samir Sedaghat.

Further Edinburgh research

All of Edinburgh's MSc Banking & Risk students undertake an authoritative piece of work over the summer and many are keen to work with a company on a 'live' project that will add value to the business. The Business School invites firms who might be interested to submit a piece of research and analysis which will be matched to one of its top-performing students. The students will be supervised by a faculty member of the Credit Research Centre.

The Business School is especially interested this year in risk modelling and banking competition. The deadline for submitting proposals is January and the work is carried out late May – August.

Contact george.littlejohn@cisi.org for more information.

All these films are available to view now at cisi.org/disruption



UNIVERSITY OF EDINBURGH
Business School

ECONOMIC CRIME

Big data and the war on financial crime

Now in its 35th year, the 2017 Cambridge International Symposium on Economic Crime, the biggest such event in the world, with some 1,600 professionals and academics attending from every continent, will this September have a special focus on City affairs, notably on the impact of big data on the rise in economic crime, and in the fight against it.

Many of the issues here revolve around the prevalence of the internet in all our daily lives. Sir Alan Yarrow, Chartered FCSI(Hon), opened his speech at the 2016 Symposium with a reference to the work of the Global Commission on Internet Governance, which had just reported.

Half of the world's population now uses the internet to connect, communicate and interact. But as the Commission points out, basic access to the internet is under threat, the technology that underpins it is increasingly unstable, and a growing number of people don't trust it to be secure. In its final report, the Commission put forward three possible scenarios for the future, and proposed key steps that everyone needs to take to achieve an open, secure, trustworthy, and inclusive internet.

The internet as we know it today will not be the internet of the future. Our actions now will determine how it evolves, for better, or for worse.

The Commission's three scenarios explore these possibilities. No matter how less than ideal, or troubling, they may be, the highly experienced professionals from around the globe who make up this elite group have put them forward as the theoretical result of everyone's choices and actions.



The Commission's first scenario, said Sir Alan, is a dark one: a dangerous and broken cyber space. The internet breaks due to malicious activity, and overreaching government regulation. Basic human rights are violated, online privacy is non-existent and government surveillance follows. Criminal data breaches are the norm and cyber attacks become more frequent. The public loses its trust in the internet and people simply stop using the network. Its potential is truly lost.

The second prospect is better – but not much: uneven and unequal gains, and stunted growth. In this second scenario, the Commission paints a picture of a future where some users are able to enjoy some of the many benefits offered by being connected, while others are permanently locked out. Freedom of expression suffers, as does access to knowledge, because governments don't preserve the internet's openness. As a result, more than three billion people are left offline. Inequality and unrest spread, with minimal co-operation by governments across borders. Sharing and innovation are limited and stifled. Many are left behind.

But then, a brighter future suggests itself in the third and final scenario, with "broad, unprecedented progress" in the Commission's words. That means an open internet that enables unprecedented progress and opportunities for individual freedom, knowledge and innovation. Billions of new users going online, narrowing digital, social, and economic divides. GDP growth reaches upwards of \$11tn by 2025. Government and industry collaborate across borders to manage the risks of online activity. This future, said Sir Alan, requires concrete actions to ensure that the internet becomes open, secure, trustworthy and inclusive for all.

The human role in cyber crime

Human error by way of a relaxed online attitude is a significant factor driving the global cyber crime threat and needs to be addressed urgently alongside technology failings. According to statistics from The Risk Management Group, 160 million phishing emails were sent daily in 2015 – 10% of these (or 16 million) penetrated conventional spam filters. However, of these 16 million, half (eight million) were read and a surprising 10% of people who read the emails (800,000 people) then clicked on links, so potentially allowing malware and virus into their computer network. A frightening 10% of people (80,000) then provided personal data.

Andrew Gracie, Executive Director at the Bank of England, recently hammered home the point that "cyber is not just about technology. More often than not attackers may seek to exploit potential weakness in personnel, to establish a bridgehead for attacks. It is therefore essential that firms have the right arrangements in place so that all staff understand cyber risk and their responsibilities for information assurance".

It is research in these areas that will be a particular focus in our next issue of *Review of Financial Markets (RoFM)*, which will feature a curtain-lifter on some current research in the fields of 'traditional' and cyber crime. If you have views on this, or anything else in this *RoFM* – or on what we should be including – then please do write to me.

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GENERATION DIGITAL – BEYOND THE ROBOTS

Michael Williamson, Cass Business School MBA 2015–16

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THE RISE OF GENERATIONS X AND Y

Digital investment advice will have the greatest impact on the next generation. So-called 'generations X and Y' will have the most buying power in the majority of European markets by the year 2025. It is very important for investment managers not only to recognise this, but also to get as much relevant investor educational information out there as possible, including on social media, in order to attract them. A 2013 survey of 4,000 affluent investors by Cogent Research of Cambridge, Massachusetts, showed that 69% of them use social media to find out financial information. This is in large part down to the emergence of smart phones and the emergence of 'mobile-native' apps that make it easy to access information on the move.



A November 2015 survey by UK research firm ComPeer of 1,000 end-investors – half in Britain and the rest spread evenly across France, Germany, Singapore, Switzerland and the US – found that 59% of US investors access their investment portfolios via a mobile application, compared to only a fifth of the Brits surveyed. Just over a third of UK investors surveyed said mobile applications are available from their wealth managers, advisers or stockbrokers. Only 17% of the remaining two-thirds want their wealth manager to launch one. But the soon-to-be-mighty buying power of generations X and Y means the industry will need to change its approach.

Almost three-quarters of the financial advisors encompassed in this research do not meet with their clients' children more than once per year, and only 20% of financial advisors pursue the younger family members of a client at all. The World Economic Forum reckons that over the next 40 years, \$41tn of wealth will be transferred to the millennials from the baby boomers, and total assets under management (currently nearing \$100tn) could be as large as \$400tn, according to Andrew Haldane, Chief Economist of the Bank of England, over the same period. Accenture estimated last year that less than half of the heirs, and the assets under management, stay with a firm after inheritance.

Investment News Data has estimated an even worse position – that two-thirds of heirs fire their parents' financial advisor after receiving an inheritance, hardly a surprise given the lack of contact with clients' children. US giants like Fidelity, for instance, are already creating teams to reach out to these families to build a relationship with the offspring. Fidelity calls its programme 'Preparing heirs'. The next generation has embraced digital channels, and will spend more time reviewing their portfolio on smartphones and other devices. On the other side of the coin, it is widely believed that two-thirds or more of

inheritance is wiped out by the receiving generation, with tax a major cause, climbing to 90% by the time the next generation takes the financial reins. These succeeding generations need a financial plan, preferably one that (legitimately) helps protect them from high taxes.

DIGITAL PLATFORMS AND REGULATION

Digital investment advice platforms will come to the fore to help solve many time-consuming issues, other than just trading for a client. The business risk of compliance will be mitigated by allowing ease of access to a client's account by the firm's compliance officer (and potentially by the regulator), which could help with the overall costs of compliance. The Financial Industry Regulatory Authority (FINRA) in the US has already taken the first steps towards mandating firms to allow access to brokers' clients electronically. Digital may become a smoother and better way for regulators to conduct oversight, especially if there are blockchain ledgers as part of this process. This should help guard against some of the inappropriate behaviours – like over-weighted single investments and churning – that regulators such as the FCA are anxious to stamp out. Reporting in November 2016 at the end of the FCA's year-long asset management market study, Chief Executive Andrew Bailey said: "We want to see greater transparency so that investors can be clear about what they are paying and the impact charges have on their returns. We want asset managers to ensure investors receive value for money through pursuing energetically their duty to act in their customers' best interests."

'Robo-advice' has received much publicity. But in the November 2016 global survey by ComPeer of 1,000 end-investors, only one in four were aware of what it actually is. Of those, though, two-thirds said they would "consider investing via a robo-adviser". That group felt that a robotic financial entity is less susceptible to making biased decisions or giving advice that is derived from traditional emotions or based on gut feeling. It is more likely to give clear and concise advice which often results in an informative decision. Others felt it added a new investment advisory service that complements their current wealth managers.

Those against the use of robo advisers commented: "[I] do not trust computers as they only work on history"; "[I] prefer an adviser who knows me and my needs"; and "[I] want to be able to discuss ideas and wishes with a real person so that I can ask them why they are making a recommendation."

Robo-advice has its place, but human advisory strengths remain important: the ability to explain complex and confusing topics, to follow up and probe based on experience, to synthesise custom client solutions, to steer clients through a difficult market and to persuade to action and provide validation. Communication with clients remains a major issue.

The ComPeer survey identified a requirement for "much improvement" in communications, with international investors proving to be more demanding in comparison to those in the UK. So we mere mortals are still in demand.

MICHAEL WILLIAMSON

With 17 years' experience in financial services in his native US, and in Australia, under his belt, Michael Williamson arrived at Cass Business School in London in 2015 to enter the MBA programme, which he completed in 2016. During this time, Michael was president of the Cass Banking and Wealth Management Society, which has more than 1,000 members, and regularly hosted events for the CISI and for Cass students, including our series of 'Great British Breakoff' debates held across the country ahead of the EU referendum. He was sponsored by a major US bank to produce his MBA dissertation on 'The future of the investment management marketplace in UK and Europe'. This paper is an updated excerpt from that dissertation, on the digital battlefield.



EXPLORING ETHICAL AND SUSTAINABLE INVESTING

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ABSTRACT¹

Ethical investment can be seen as falling into the 'nice-to-have' but not essential category. This paper seeks to raise awareness of the fundamental importance of ethical investing and to increase familiarity with the concept of 'sustainable' investment. It includes a brief history of the topic and outlines a number of approaches that can be used to help counter assumptions that it simply involves excluding 'sin stocks'. In practical terms, ethical investors may benefit from an awareness of resources available as well as some suggestions to help differentiate committed ethical investment fund managers from those seeking a marketing advantage from a green makeover. Finally, the logic behind assumptions that ethical investments must underperform due to 'the price of conscience' is challenged, with emphasis on the interplay between ethical investing, risk and competitive advantage.

INTRODUCTION

Although ethical investment can be seen as desirable but not essential, this paper outlines its fundamental importance and outlines 'sustainable' investing, a more recent development. Having established sustainable investing's significance, implementation approaches are outlined, moving beyond common assumptions that it only involves avoiding investment in companies carrying out unacceptable activities ('sin stocks'). In practice, ethical investors can benefit from awareness of resources available as well as approaches to help identify committed ethical investment fund managers from those seeking a marketing advantage from appearing ethical ('greenwashing'). Finally, investors may believe that ethical restrictions placed on the investment opportunity set must result in inferior performance, the so-called 'price of conscience'. This logic is challenged by exploring the interplay between ethical investing, risk and competitive advantage.

ETHICAL INVESTING MATTERS

The relationship between sustainability and finance usefully sets the background to ethical investing.

Unsustainable human activities have generated threats including climate change, resulting in damage, loss of life, and disruption to food and fresh water supplies. The human life-span is increasing, so demographics will impact healthcare and pension costs. An expanding proportion of a growing world population will demand improved living standards as less developed countries modernise. Proponents of responsible investment argue that behaving in an unsustainable manner will cease to be an option.

Corporations are ubiquitous and powerful, spanning the globe. Humanity needs them to end unsustainable behaviours and tackle future challenges, which may include environmental challenges, climate change and social

issues. Regrettably, part of industry's dynamism has been (and still can be) the externalisation of costs on to the environment, communities, employees or future generations [1]. Financial markets help support and control corporate behaviour; markets reward ingenuity, efficiency, talent and productivity through the ability to raise funds and by share pricing (thereby valuing companies). Companies making far-sighted investments tackling these problems will benefit in either the short or longer-term, making them valuable investments.

Since corporate activity is an essential part of human activity and development, sustainable investment also requires that companies generate economically sustainable long and short-term returns. This counters short-termism, where immediate profits are made at the expense of damaging profitability at a later date.

In today's environmentally and socially aware business environment, there is appreciation that:

- Companies taking environmental risks have caused disasters (eg, oil spills, deforestation, mining pollution).
- Social costs of business practices can no longer be ignored, as in previous eras.² Public tolerance of unacceptable worker conditions has diminished (eg, labour conditions in mines and child labour).
- Companies require effective governance to confidently develop, meet legal and ethical requirements, and be accountable to stakeholders, including owners and shareholders. Corruption facilitates losses and sub-optimal decision-making. Poor oversight encourages high-risk behaviours and damaging scandals, potentially undermining reputations of entire industry sectors.³

In the modern technologically-enabled world, environmental, social and governance failures are readily exposed by media and achieve global coverage rapidly. Such failures can easily result in financial losses, adverse litigation, reputational damage and clients taking business elsewhere. This has the potential to cause enormous damage to a company's value, share price and even its long-term survival.

Thus ethically and sustainably orientated companies have the opportunity to target higher long-term profits by addressing necessary challenges while avoiding failures. At the same time they should accumulate marketing advantages and loyal customers as a result of their ethical behaviour.

SUSTAINABLE INVESTING

For current purposes, little distinction is made between ethical investment, socially responsible investing or sustainable investing.⁴ Companies are encouraged to promote practices including environmental stewardship; consumer protection; human rights and support the social good [2], [3]. One focus is on environmental, social justice and corporate governance issues (ESG). In sustainable investing, funds are directed into companies with business practices capable of being continued indefinitely without causing harm to current or future generations, or exhausting natural resources (ie, not 'unsustainable'). Sustainability is often defined as ensuring development meets the needs of the present without compromising the ability of future generations to meet their own needs [4].

ESG identifies three key dimensions of sustainable investing (see Figure 1).

1. Environmental, including CO₂ emissions, or carbon-intensity; forest and woodland degradation (important for absorption of atmospheric

1. The paper includes numerous endnotes, too many to publish in print. Some are included here as footnotes, but please refer to cisi.org/rofm-jan17 for the complete listing.

2. For example, the slave trade.

3. For example, the LIBOR scandal undermined the reputation of banking and finance [19].

4. For brevity, in this article the term 'ethical' investing will generally be used interchangeably with 'socially responsible investing', 'responsible investing' and 'sustainable investing' except in cases where a useful distinction can be drawn. Definitions of these terms are offered in [2].

CO₂); airborne, water-borne or land-based pollution; usage of scarce resources, including water and living creatures as well as minerals, oil and natural gas; mining activities which generate toxic byproducts; over-fishing, intensive agricultural methods and so on.

2. Social, including corporate social responsibility (CSR); child labour; modern-day slavery; payment of non-living wages; hazardous, exploitative and/or coercive working conditions;⁵ structures that reduce corporate taxation bills to levels incommensurate with the profits and activities taking place in those countries; anti-social working hours or conditions; displacement of indigenous peoples.
3. Governance; companies with weak internal controls may have management not following company policies, increasing risks of irresponsible behaviours, corruption and bribery. At board level, weak governance may mean that non-executive directors (NEDs) are unable to hold powerful executive directors in check, with possible damage to the company as well as the owners' (shareholders') interests, and increased risk of excessive executive remuneration.

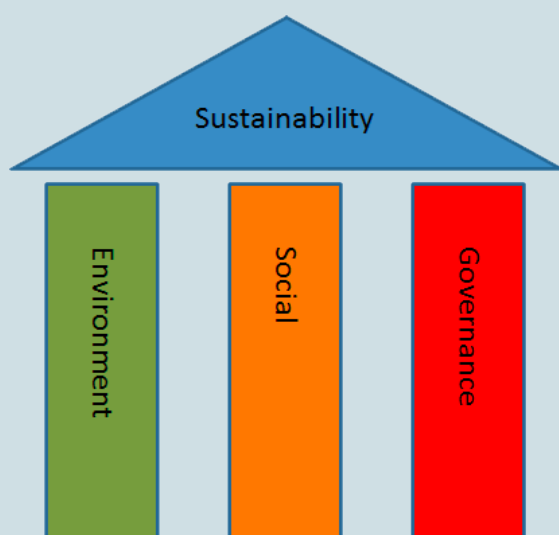


Figure 1: The three pillars of sustainability

Companies may outsource production to countries or other companies operating without meaningful sustainability practices. A company might claim ethical operations, while not looking too deeply into its suppliers' practices. Best practice requires companies to scrutinise their resource chains and monitor the entire production process, from origin through to ultimate disposal of products after use.

Companies may externalise costs of production [1]. Companies consume resources and create waste products. Ideally all costs associated with resources consumed and waste product disposal during manufacture would be included in the price of goods created; including disposal after use.

A company with energy-intensive production, burning fossil fuel, may release significant quantities of atmospheric⁶ CO₂. The build-up of atmospheric CO₂ is leading to global warming and climate change. This is unsustainable, yet it is generally unlikely that the company releasing

CO₂ will be paying significantly towards atmospheric CO₂ reduction, or pricing the cost of CO₂ removal into the finished product. The costs of climate change adaptation will fall to society as a whole, often with poorer countries suffering greater damage (and costs) than richer, industrialised countries.⁷ This typifies externalised costs: the company that emitted the CO₂ has not paid for its consequences. Generally consumers buying that company's goods may not pay a price reflecting the true cost of dealing with the CO₂ involved in production.

Externalising production costs applies not only to pollution; similar arguments relate to forcing labour to subsidise activities, and saving money with potentially health-damaging practices or inadequate wages. Failure to invest in appropriate governance and management structures can result in company staff undertaking activities boosting earnings, but with the tab ultimately being picked up by society or taxpayers. The company saves money on management and governance, while the taxpayer pays the cost of dealing with problems that may arise as a result. The company externalises these costs to the taxpayer when it should pay them itself.

Having identified some concerns motivating ethical investing, investors want, broadly speaking, to see capital put to an ethically good use. Not merely maximising investment return, but also causing benefit (or at least doing no harm) while generating a decent return, 'doing well while doing good'.

Ethical investors wish to allocate resources to areas they feel deserve investment and to avoid businesses that (directly or indirectly) do not. Typically avoiding the so-called 'sexet of sin', which generally refers to alcohol, tobacco, gambling, pornography, armaments and nuclear power [3]. Different investors may wish to avoid different or more sectors than these.

Exclusions, or 'screening' is only one strategy of several. Consider:

- Do investors wish to avoid unethical companies, but accept ethically-neutral companies doing neither good nor harm? (Negative screening.)
- Do investors wish to invest only in ethical companies, avoiding both unethical and ethically-neutral companies? (Positive screening.)
- Do they wish to actively seek to influence corporate behaviours for the better? (Positive engagement, or shareholder activism.)

These questions and their implementation lead to a nuanced range of investment approaches.

HISTORY OF ETHICAL INVESTING

Malthus's 1798 'Essay on the principles of population' warned of population growth outpacing the planet's ability to support human needs [5]. Including social aspects to business activity dates from the 1700s, with mutual societies and Quaker philanthropists such as Cadbury's. In the 1800s the Quakers prohibited members from participating in the slave trade. Ethical investing also traces thinking from Methodism.⁸ Its religious roots meant investors were asked to avoid companies encouraging 'sin'. Association with guns, liquor and tobacco were to be avoided.

Over time, the list of excluded business widened to include social and environmental problems [6]. The 1972 Stockholm Conference on the Human Environment named the environmental assessment component

5. More recently in the developed world, this may also extend to the use of 'zero-hours' contracts, in which the employer is not obliged to provide any minimum working hours, while the worker is not obliged to accept any work offered. Unions have raised concerns about the possibility of exploitation, since management could use these contracts to reward or punish employees for any or no reason, and whether workers would be able to adequately assert their rights.
6. And potentially other pollutants, such as sulphur.
7. Which have historically benefited from the industry that generated much of the CO₂ in the first place.
8. John Wesley's sermon on the topic of the 'Use of money', published in 1872, set out the principles of social investing. He invited his fellow worshippers and investors to not harm their neighbour through their business practices and to avoid certain industries.

of its action plan ‘Earthwatch’, recommending environmental assessment as an operational area of the UN Environment Programme (UNEP). Business pioneers such as The Body Shop (1976) and Ben & Jerry’s ice cream (1978) placed ethical and social considerations deep within their offering [7]. The Stockholm recommendations were elaborated in the 1980 World Conservation Strategy – a collaboration between the International Union for the Conservation of Nature, the World Wildlife Fund and UNEP. In 1983, growing realisation in national governments and multilateral institutions of linkage between economic development and environmental issues lead to establishment of the World Commission on Environment and Development by the UN General Assembly. Depletion of the atmospheric ozone layer by chlorofluorocarbons lead to the 1989 Montreal Protocol ban. In 1992, leaders set out sustainable development principles at the UN Conference on Environment and Development in Rio de Janeiro, Brazil.⁹ Later in 1992, the UN General Assembly officially created the Commission on Sustainable Development. The 2006 Stern report [8] concluded that the benefits of decisive early action on climate change outweighed the costs. In 2007, the International Panel on Climate Change declared “it is no longer a question of whether climate change policy should be understood in the context of sustainable development goals; it is a question of how”.

Ethical investing’s history means several excluded sectors derive from religious roots, while civil nuclear power’s association with atomic weapon development may taint that sector, despite its ability to reduce CO2 emissions. Sustainable (ESG) investment may be a useful development: by emphasising the need for sustainability, ethical investment can be placed on a more scientific basis, without the need to lean upon its religious roots.¹⁰ The identification of ESG factors gives clarity of focus, provides structure, and potentially the addition of further factors if desirable.¹¹

INVESTMENT APPROACHES

Investments tend to focus on activities that are seen as generating desirable or undesirable outcomes. Sustainability is helpful when it comes to determining where an activity should be seen as having a positive or negative impact, based on ESG factors.

Ethical investing means different things to different people and institutional investors may answer to stakeholders that differ amongst themselves. Despite the range of approaches available, some investors may feel that none of the main methods fit their requirements. Approaches commonly use screening, but can also use ‘best-in-class’, tilting, or influence and engagement.

Screening

Screening appears to be the commonest approach. Investments are tested against several requirements aligned with positive and negative impacts, or other criteria. Companies’ impacts are identified as positive, negative, or ‘ethically-neutral’ (broadly doing neither good nor harm).

Following screening, an investor must decide whether to avoid ethically-neutral companies (see Figure 2).

- Negative screening avoids unethical companies, but invests in ethically-neutral companies.
- Positive screening only invests in ethically beneficial companies, avoiding ethically-neutral and unethical companies.

9. Three instruments of environmental governance were established: the UN framework Convention on Climate Change (UNFCCC), the Convention on Biological Diversity (CBD) and the non-legally binding Statement of Forest Principles.
 10. A religious basis for ethical investing could create disagreements about what can be regarded as ethical. For example, Islamic finance may prohibit payment of interest, meaning that conventional interest-paying bonds would be unacceptable, although acceptable to some other religions.
 11. Many current debt levels, both nationally and in companies, may be regarded as unsustainable, potentially providing exclusions for sustainable investing purposes. This suggests the possibility of adding further factors beyond ESG to sustainable investing, perhaps relating to debt or corporate financing, although academics and practitioners would need to debate what level of debt should be regarded as ‘unsustainable’. In a similar vein [3] suggests five factors.
 12. Perhaps with a higher price-earnings (PE) ratio compared with their sector average, or access to cheaper debt financing for example.
 13. Apart, presumably, from winding the company’s operations up.

A concern with screening is that it can generate portfolio biases towards company size and sectors, limiting portfolio diversification.

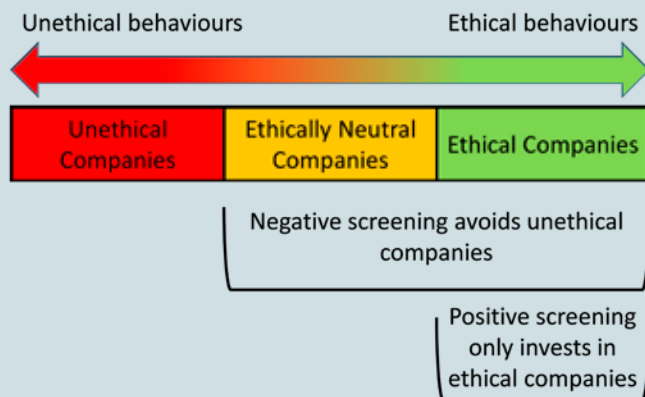


Figure 2: Positive and negative screening

Best-in-class

This approach includes companies and industries that are the best operators within the class considered, including the best companies within a sector. This can mean selecting the ‘least bad’ companies in that sector.

It can motivate companies in ethically-challenging sectors to improve. Consider the position of a fictitious mining company against some different ethical investing strategies. Suppose our mining company has a weak record with regard to environmental damage during extraction, pollution from refinery waste products, treatment of labour and of indigenous peoples displaced or harmed by its activities. If financial markets reward superior sustainable practices:¹²

- Positive screening excludes the company based on sector, which would likely be unacceptable. Management can take no action to make the company acceptable.¹³
- Negative screening would similarly exclude the company, due to its sector.
- Under best-in-class, the ‘least bad’ companies in the sector can attract investment. By comparing with peers, management can improve their environmental and social record to be amongst the best in their sector and attract investment. In a competitive market environment, this can motivate companies in a ‘race to the top’, thereby generating real improvements for those affected by the company’s activities, even if they will never be perfect.

The company could also be influenced by ethical investment styles such as ‘tilting’, if they can reduce their carbon intensity, influence and engagement or shareholder activism.

For investors seeking to actively engage, best-in-class can provide benefits to those most affected by negative company practices.

Portfolio tilting

Data providers can supply information on ESG scores or the carbon-intensity of portfolio holdings. Determining whether, for example, a portfolio is over or under-weight its benchmark in terms of carbon intensity.

In this more nuanced approach, a portfolio is tilted away from carbon-intensive sectors or companies towards lower carbon areas. For investors wishing to be somewhat 'green' but fearing that ethical investing might undermine performance,¹⁴ this offers a 'light green' approach. Some exposure towards carbon-intensive areas is permitted, provided that elsewhere, sufficient weight is given to low-carbon industries, and overall the portfolio has a lower carbon intensity than its benchmark index. The manager can allocate across a wide range of companies or sectors to help with diversification and performance.

Influence and engagement

This approach involves influencing company directors, where appropriate, to make improvements in matters of ethical concern [3]. Directors are encouraged and supported to improve the balance between risk and return in the best interests of long-term owners.

The process may involve management meetings, questionnaires, and collaboration with other fund managers. The intention is to influence companies to consider their responsibilities to the environment, their stakeholders¹⁵ and society as a whole.

INFORMATION SOURCES

Apart from investment approach, an investor must select ethical companies and monitor their performance. Corporate carbon emissions, social responsibility and governance quality are not easy to measure objectively. Consequently, ethical investing is often outsourced to organisations with specialist skills, with many investors employing the skills of specialist fund managers.

Information sources tend to depend on whether investing via funds or directly constructing a portfolio that meets ethical criteria.

Ethical funds

Several fund management houses run ethical investing strategies. Some specialist houses only run ethical funds, while others include ethically-orientated funds as part of their wider offering.

A concern for investors is whether fund managers lack ethical investing experience, but want to 'jump on the bandwagon', launching a fund to appeal to the ethical market. Examination may reveal that although promoted as such, a fund's ethical credentials are slender, potentially including holdings (or an approach) that clients would not regard as particularly ethical. A company lacking experience may launch a new ethical fund, but fail to reach required assets under management (AUM) targets to make it economically viable. This could result in a merger with a conventional fund, closure, or a shift away from ethical objectives. Inexperience with ethical investing could mean insufficient resources (such as databases on ethical activities and carbon intensity) have been allocated to develop the fund or insufficient investment in experienced staff with the necessary training and qualifications. This could result in inability to deliver the performance expected, resulting in gradual erosion of interest in the fund, with consequences such as closure, merger and change of objectives.

14. The price of conscience.

15. Which may include staff, customers, shareholders and those living near their centres of operation.

16. International Standards Organisation: ISO 26000 on social responsibility, ISO 14000 on environmental management, as well as standards in energy management, occupational health and safety, and anti-bribery.

These concerns can be partially addressed by selecting funds from specialist ethical management houses. Their objectives and track record are likely to be more clear-cut. Good questions to ask when selecting an ethical fund might include:

- Does the fund house specialise in ethical investing, or does it manage other conventional funds?
- How deeply embedded is ethical investing culture in the organisation? What specific ethical initiatives does the fund management house undertake? How ethical are its own corporate values? Does it practice what it preaches?
- How long have they been running ethical funds for? What is their style and track record like?
- How long has the fund been running? What ethical investing style does it use?
- What resources do the managers have access to? What databases are used to investigate companies for investment? Are analysts proactive in contacting companies? Are shares' voting rights used to influence companies invested in?
- What ethical investing experience and qualifications do staff have? Fund management houses may find clients like to hear them talk positively about ethical investing, and may do so for marketing benefits. Questions that explore the genuine level of staff experience may help detect those with only 'skin deep' commitment. Ethical investing qualifications appear in relatively short supply; only organisations and staff seriously committed are likely to have individuals with specific qualifications from recognised training institutions and accepted by industry bodies.

A number of organisations and companies offer resources that can assist investors in determining the ethical credentials of specific funds and fund management houses (such as Morningstar and SRI Services).

Individual companies, corporate standards and initiatives

A manager constructing a portfolio of ethical companies faces different challenges. Portfolio construction may use both ethical funds and individual stocks; requiring additional perspective on funds or companies.

When considering a company for portfolio inclusion, apart from return, risk and diversification aspects, the manager must consider whether it meets ethical investment objectives. Although some criteria (like screening and carbon intensity) might be straightforward, other requirements could be sector specific.

Portfolio managers are assisted by corporate standards introduced in different countries over several years, including some ISO standards.¹⁶ Many are voluntary, but confirm that certain activities have been conducted meeting defined standards. While such standards are helpful, the sheer number can be difficult, and requirements vary. Often sustainably-orientated companies seek to meet requirements and be audited for several standards, even if related; thus adoption of multiple standards covering a company's operations can provide some reassurance. However, the portfolio manager might be well advised to explore the differences between standards and how they are independently audited before reaching final conclusions. Other questions regarding standards are whether they provide symbolic or real value and whether they are strong but voluntary [5].

Independent organisations have launched initiatives encouraging companies and organisations to behave more responsibly, ranging from auditable quasi-official standards to reporting initiatives encouraging

companies to publicly report emissions, achievements and progress to motivate them and others to improve.

One information source is company annual reports and accounts. These should reveal not only the company's stated ethics, sustainability, CSR, environmental objectives and corporate standards, but also information about corporate governance [9], [10]. Several years' of reports and accounts should be examined, exploring such aspects as tenure and role of NEDs, board turnover, expertise, genuine level of independence, ability to challenge executive decision-making, and composition and independence of the remuneration committee. Resources covering environmental factors cover issues related to environmental concerns, including agriculture, emissions, energy, and water.

For CSR, apart from resources covering labour and social issues, one test is to compare the salary of the highest paid staff member to the lowest paid as a measure of labour equality within an organisation [1].

Investors must dig beneath superficial statements regarding company achievements in these areas, since many companies desire a 'green makeover', while reluctant to absorb the costs and challenges required for genuine change [3]. The finance sector has come under scrutiny following scandals in recent years, and has a crucial role to play in encouraging sustainable investment, with organisations promoting such activities. It is also worth exploring the wider topic of sustainability for economies and businesses.

INVESTMENT PERFORMANCE

Investors seeking a performance yardstick for ethical funds or portfolios can use ethical indices, including those run by Dow Jones and FTSE indices. A major question is how ethical and conventional investments compare, with concerns about underperformance, further clouded by worries that 'ethical' or 'green' labels have been applied for marketing advantage. The problem is distinguishing between fund providers with only superficial commitment to ethical investing and those with genuine commitment and skills. Careful examination of fund and provider is required to help determine whether there has been a 'green makeover' for marketing purposes, or whether it can really deliver the ethical requirements desired.

Beyond ensuring selection of genuine ethical funds, there remain questions about whether such funds must underperform in the wider market. Investors often perceive ethical investing as positive or negative screening. Since this reduces the number of companies available for investment, the smaller 'opportunity set' reduces diversification possibilities, resulting in worse returns, higher risk, or weaker risk-adjusted portfolio performance. The following sections propose arguments challenging this perception, not by data analysis (it can be difficult to prove persistent performance tendencies from finite datasets), but by raising counter-arguments intended to widen debate. The counter-arguments relate to sustainable investing and risk, and whether sustainable investment can give competitive advantage [1], [11].

Sustainable investing and risk

It can be difficult to prove that one investment style or another is superior over an extended period. Proponents of sustainable investing argue that unethical corporate behaviour and unsustainable practices lead to increased risk [3], [11]. Harmful behaviour by companies eventually leads to negative consequences for them, generally having a detrimental effect on growth, profits and share price, leading to market underperformance, thereby running risks that are not well reflected in share price (not 'priced in' by the market). By excluding these companies, an investor is removing sources of unrewarded risk from their portfolio.

Such practices can increase the likelihood and consequence of litigation against the company, cause reputational damage to brand or products, or make customers decide they do not wish to be associated with the company and take business elsewhere. Other risks that can be very real in a competitive corporate environment may include:

- Poor industry standards stimulating increased government regulation in affected sectors, increasing business costs to all companies in that sector [12]. Those firms that have invested least in meeting, maintaining or raising standards will be most affected, as they are forced to improve.
- National or international environmental issues, such as climate change causing CO2 emissions restraints or carbon permit trading [8], [12]. Companies investing in appropriate technologies are better placed to adopt new standards and avoid heavy redesign costs, while those continuing harmful emission practices may require significant investment or higher ongoing business costs.
- Ethical behaviour gives a company a social 'licence to operate', being accepted as a valued community asset, avoiding opposition or resentment about activities [11]. Community, government and NGO opposition can upset projects and damage company brands. Brand risk can be significant – oil-spills can cause reputational damage lasting decades.
- Poor sustainability records can increase insurance premiums, increase the cost of capital, or make it unavailable. Investor concerns about sustainability can increase the cost of debt and equity (lower share prices) [11].
- Unethical supply-chain partners can tarnish the reputation of a company's brand [5].
- Energy usage reduction and waste minimisation helps optimise corporate processes, increasing efficiency and reducing costs.

Other business risks include [11]:

- Operating risks involving emissions and waste discharges, risks involved with product liability, permit costs and 'eco-taxes'. Particularly affecting companies in the mining, oil, gas and forestry sectors.
- Balance sheet risks. Historical and contingent liabilities can negatively impact corporate market value. Decommissioning mines and cleaning up derelict industrial sites can be burdensome without suitable preparations. Litigation threats can damage stock price.
- Capital cost risk, involving pollution control expenditures, product redesign and other outlays following changing environmental standards, regulations and customer expectations.
- Business sustainability risk. Companies may face risks associated with the intrinsic lack of sustainability of their activities. Examples include coal mining, especially high-sulphur coal producers.

Competitive advantage

A businessman (or investor) may question whether ethical behaviour is profitable, or assume ethical behaviour has a cost. However, an ethical company should be able to build a good reputation, bringing financial rewards [13], [14]. Ethics encourages businesses to earn legitimate profits, contributing to society, avoiding coercive, exploitative or illegal practices (after all, a protection racket is a type of business). Internationally this relates to countries with lesser standards for human rights, labour, bribery and the environment [15].

An honest and trustworthy reputation attracts customers and potential business partners, creating economic opportunities [16]. Staying within the letter of the law is insufficient to protect reputation: not everything immoral is illegal. Laws can be slow to respond to new social concerns. An ethical climate within an organisation helps protect it from unethical

or illegal staff conduct, since strong ethical principles help limit abuses by staff who may be tempted to circumvent regulation. Individuals in a modern international workforce have differing backgrounds, cultures and perceptions of what constitutes acceptable behaviours. They may be under pressure, while facing decisions that affect their own interests.

To trade and deal effectively, companies require trust, quality of goods and services, employees' rewards, and a return on investors' capital. Many financial products depend upon standardised contracts and deliverable product, including terms associated with futures contracts, which are highly standardised. Additionally, companies with stronger ethical reputations should command higher PE ratios for their stock and borrow at lower rates in bond markets [17].

A 2010 study [18] concluded that positive CSR strategies were initially perceived as being value-destroying by analysts but have moved to being value-creating, with positive impacts on stock recommendations. Analysts are now more likely to recommend a stock 'buy' for strong CSR firms.

Other sources of competitive advantage for superior ethical performance, which can add value, ultimately being reflected in market pricing include [11]:

- Attracting, retaining and motivating top talent.
- Anticipating changes in the regulatory and business environments ahead of competitors.
- Generating revenue growth through new products, services and technologies.
- Increasing customer and investor loyalty.
- Improving relations with regulators, local suppliers, communities and key stakeholders.
- Securing, retaining and enhancing a 'social licence to do business', particularly in emerging market countries.
- Reducing operating expenses through improved energy efficiency and waste minimisation.
- Reducing the risk of legal liabilities and fines.
- Accessing and affording greater investment capital (through enhanced share prices and reduced cost of debt).
- Improving innovation and adaption within the corporate culture.

SUMMARY

To raise awareness and promote discussion around ethical investment, this paper outlines the fundamental importance of the topic before introducing sustainable investing and ESG factors. Following a brief history, it overviews approaches that can be used to help counter assumptions that it only involves excluding 'sin stocks'. It also outlines resources available to ethical investors and suggestions to help identify committed ethical fund managers. Finally, the assumption that ethical investments must underperform due to 'the price of conscience' is challenged by considering ethical investing in terms of risk and competitive advantage.

QUINTIN RAYER, CHARTERED FCSI, DPHIL (OXON)

Quintin Rayer, Chartered FCSI, is a Chartered Wealth Manager. He holds a Physics degree from Imperial College London and a Physics doctorate from Oxford University. Quintin has applied knowledge from nuclear and aerospace engineering to areas in finance, working for actuarial and investment consultancy firms as well as a multinational European bank for nearly ten years. Projects have included substantial and innovative development of quantitative fund selection and analysis techniques, risk monitoring and portfolio optimisation, including in-house training for analysts and relationship managers. Quintin has completed the Sustainable Investment Professional Certification (SIPC) with the John Molson Business School, becoming this programme's first graduate in the Channel Islands and the second in the UK.



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THE SPACE VALUE OF MONEY

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In September 2015, 193 world leaders agreed to 17 'Global Goals for sustainable development'. If these Goals are completed, it will mean an end to extreme poverty, inequality and climate change in less than a generation. To attain these Goals by 2030 we must reel in the vast pool of capital currently deployed outside the guidelines of sustainable investing. To achieve this, we need to transform our mainstream risk and time-based financial models. Dr Armen Papazian proposes a new principle of value, 'Space Value of Money', and new metrics of value that would seamlessly extend our existing equations, integrate impact and return, and provide us with a space value optimisation tool aligned with these Global Goals.

SPACE VALUE OF MONEY

Space Value of Money establishes our spatial responsibility to ensure that a dollar invested in space has, at the very least, a dollar's worth of positive impact on space.

Net Space Time Value (NSTV)=Net Present Value(NPV)+Net Space Value (NSV)

$$NSTV = -II + \sum_{t=1}^n \frac{CF_t}{(1+r)^t} - II + \sum_{t=0}^n CE_t(1+s)^{n-t}$$

$$NSTV = -2II + \sum_{t=1}^n \frac{CF_t}{(1+r)^t} + \sum_{t=0}^n CE_t(1+s)^{n-t}$$

$II = \sum CE_t =$ Sum of Cash Expenditures

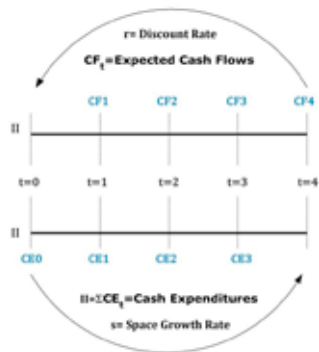
$CF_t =$ Future Expected Cash Flows

$n =$ Project Timeframe

$s =$ Space Growth Rate

$r =$ Discount Rate

$t =$ Moving time



INTRODUCTION

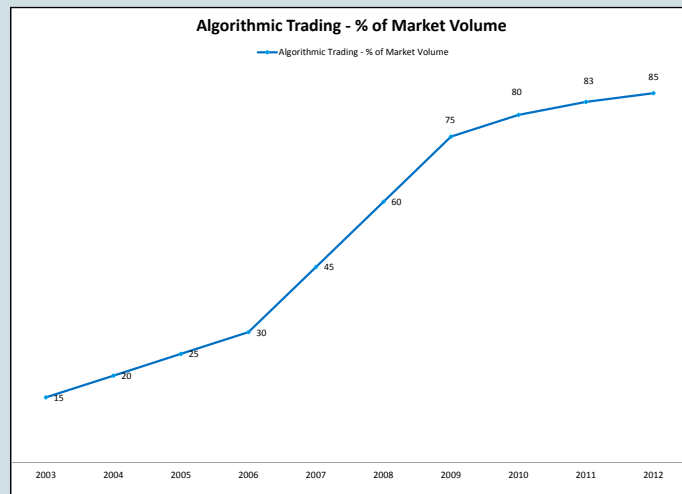
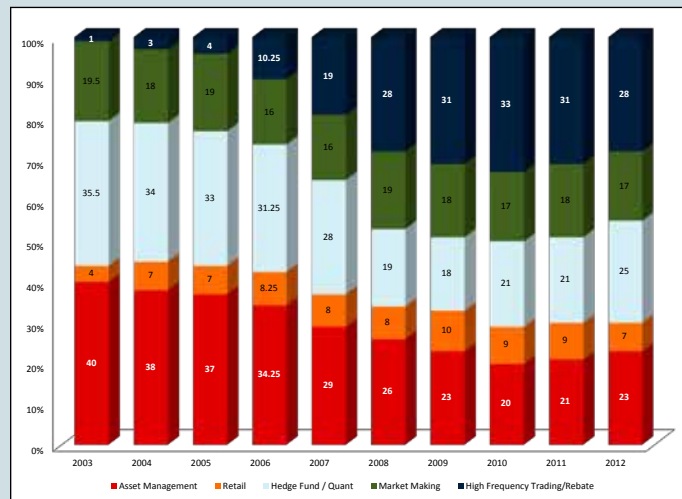
The market share of sustainable investment strategies has been growing steadily over the last few years. Between 2012 and 2014, global sustainable investment assets grew by 61%, from \$13.3 to \$21.4tn. In this same period, the proportion of total professionally managed assets that were deployed based on sustainable investment strategies increased from 21.5% to 30.2%. This means that in 2014, 69.8% of all professionally managed assets were *not* invested according to sustainable investment

1. GSIA, *Global sustainable investment review*, 2014.
2. James Davies, Rodrigo Lluberas, and Anthony Shorrocks, *Credit Suisse global wealth databook 2015*.
3. GSIA, *Global sustainable investment review*, 2012 and 2014, identify the following seven main approaches: 1) negative/exclusionary screening, 2) ESG integration, 3) corporate engagement and shareholder action, 4) norms-based screening, 5) positive/best-in-class screening, 6) sustainability themed investing, and 7) impact/community investing.
4. Robert Kissell, *The science of algorithmic trading and portfolio management*, Academic Press, 2013.

strategies.¹ Meanwhile, by mid-2014, total global wealth was estimated at \$262.6tn.²

While we are making great progress, if we are going to attain our Global Goals by 2030, we must reel this vast pool of capital into the fold. To achieve this, we must transcend our risk/time models, and build on and expand our current approaches to sustainable investing.³ This is due to the limitations of our risk/time paradigm, and the rise of algorithmic trading, which has made programmability a key to the success of any type of investment strategy (Charts 1 and 2). With the rise of fintech and blockchain, this trend is set to grow further, deeper and wider.

Charts 1 and 2: Algorithmic trading as percentage of market volume and market participants (US)⁴



Building the 2030 world according to our Global Goals will require a number of important changes in the way we measure, design and value our investments. We will need to address impact and return together, and allow investors the opportunity and possibility of optimising their space impact in line with our Global Goals, across projects and different asset classes, using the latest technology.

This paper proposes a new analytical tool for Space Value Optimisation that can help finance functions design and value investments in a way that optimises their space impact, and maximises the positive contribution to our Global Goals.

The Space Value Optimisation tool fills an important market gap, and supports the widespread implementation of ecologically and socially sound investment models and algorithms that are seamlessly integrated with our current models.

CURRENT VALUE FRAMEWORK

Our current financial value paradigm is built on two principles, Risk and Return and Time Value of Money, which describe a universe where time and risk parameters define the value of an investment opportunity or a series of expected future cash flows.

$$Net\ Present\ Value = -II + \sum_{t=1}^n \frac{CF_t}{(1+r)^t}$$

Using the Net Present Value equation as an example, we can see that the model discounts the future expected cash flows to the present with a discount rate *r*, which is the opportunity cost in the form of the return on an alternative investment with the same level of risk.

The equation applies time and risk parameters to the expected cash flows in the future (*t* and *r*), and leaves the Initial Investment (II) as an abstract theoretical sum to be subtracted from the present value of the imaginary cash flows in the future.

The equation does not consider the *impact* of the II, which, when and if addressed, is addressed outside the key parameters of the model, as an externality.

Having the nature and space impact of the Initial Investment in its blind spot, this model is effectively incapable of distinguishing between a solar-powered asteroid mining company and a coal-powered cement factory.

THE MISSING PRINCIPLE: SPACE VALUE OF MONEY

Space Value of Money is built on the observed premise of reciprocity between our thoughts and actions, and what happens to and in space. Indeed, what goes around comes around, and as we think, design, choose and define our actions in space, we define our impact on space.

Space Value of Money establishes our spatial responsibility to ensure that a dollar invested in space has, at the very least, a dollar's worth of positive impact on space.

Space Value of Money complements Time Value of Money and Risk and Return, and requires that *while we are maximising our returns and minimizing our risks, we also optimise our space impact.*

THE NEW METRICS OF SPACE VALUE

The Space Value metrics help us fulfil this responsibility by treating the impact of the II as an integral element of the value of the investment, and thus of the investment decision. Gross Space Value (GSV) provides an assessment of the aggregate space impact of an investment taking into account the New Assets (NA) and New Money (NM) that the investment will create, and its Carbon and Waste Footprint (CF and WF).

$$Gross\ Space\ Value\ (GSV) = Initial\ Investment\ (II) + New\ Money\ (NM) + New\ Assets\ (NA) \pm Carbon\ Footprint\ (CF) \pm Waste\ Footprint\ (WF)$$

$$GSV = II + NM_n + NA_n \pm CF_n \pm WF_n$$

n = Project Timeframe

$$NM = New\ Money = II * DR * BLR + (II + X - M) * mm$$

mm = Money Multiplier, *DR* = Debt Ratio, *BLR* = Bank Loan Ratio, *M* = Imports, *X* = Exports

$$NA = New\ Assets = aINV + bRE + cT + dIP + eFIN + \dots$$

a, b, c, d, and e = Coefficients

INV = Inventories, *RE* = Real Estate, *T* = Technology, *IP* = Intellectual Property, *FIN* = Financial Assets

CF = Carbon Footprint = CO2 Equivalent Emissions in Toones of CO2 * Verified Carbon Unit Price

WF = Waste Footprint = Waste Output in Tonnes * Cost of Treatment per Tonne

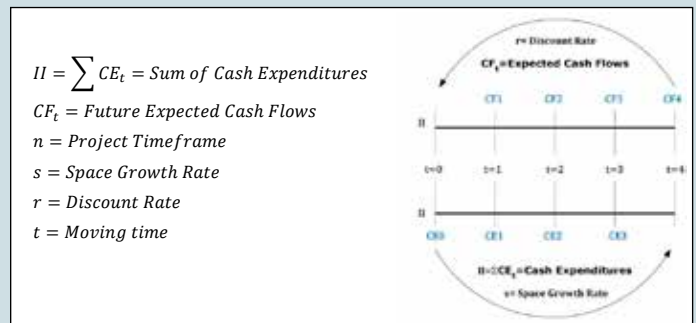
$$Net\ Space\ Value\ (NSV) = Gross\ Space\ Value\ (GSV) - Initial\ Investment\ (II)$$

Net Space Time Value (NSTV) brings into one equation the risk time metric Net Present Value and the space time metric Net Space Value, providing us with an aggregated measure of the space and time returns of the investment, while accounting for risk. It also introduces the Space Growth Rate, which reflects an investment's present and/or planned impact in monetary terms, from II to GSV.

$$Net\ Space\ Time\ Value\ (NSTV) = Net\ Present\ Value\ (NPV) + Net\ Space\ Value\ (NSV)$$

$$NSTV = -II + \sum_{t=1}^n \frac{CF_t}{(1+r)^t} - II + \sum_{t=0}^n CE_t(1+s)^{n-t}$$

$$NSTV = -2II + \sum_{t=1}^n \frac{CF_t}{(1+r)^t} + \sum_{t=0}^n CE_t(1+s)^{n-t}$$



SPACE VALUES AND GLOBAL GOALS

Setting a required space growth rate for a project has practical implications for the investment, its management, and execution. By setting a positive space growth rate target, we are in effect requiring that the investment's new money and new asset impact, as well as its ecological and waste footprint, are designed in line with our Global Goals.

Indeed, much like discount rates, a benchmark Space Growth Rate can be defined as a target rate across an economy. This provides governments the opportunity to prove their commitment to the environment and set high standards of Space Growth Rates for public investments, thus raising the bar for private investments.

Directly impacts



Indirectly impacts



The Space Value Optimisation toolkit allows the finance function to define its own unique equation for New Money and New Assets.

For example, one could decide to attach a monetary space value to employment/personnel, even though the latter is not categorised as an asset under our current accounting standards. This could be achieved by adding $gEMP^5$ to the New Asset equation, and assigning relevant coefficients that reflect our goals regarding factors such as gender balance, full time employment, fair wages, benefits and education.

The assets and their mode of creation and utilisation make the difference between a positive and a negative space growth rate. For example, when valuing a defence or oil company, we face an important question regarding the value of their inventory. The inventories of these firms, when used, have a proven track record of negative space impact, spreading pollution, destruction, and a host of other negative effects diametrically opposed to our Global Goals.

Indeed, what would the value of oil and defence companies be, if we were to integrate the impact of their inventory on the planet into our value models?

It could be argued that, in fact, if we are ever going to achieve our Global Goals, oil and defence companies should be assigned an inventory coefficient of at least -1, as the damage they cause could actually be far greater than the value of their inventory.

OTHER APPLICATIONS

In November 2015 the US Senate passed legislation H.R.2262, which states: "Any asteroid resources obtained in outer space are the property of the entity that obtained them, which shall be entitled to all property rights to them, consistent with applicable federal law and existing international obligations."

The Space Value Optimisation tool supports the growing ambitions of humanity, and provides a framework that integrates our spatial responsibility and spatial expansion plans.

CONCLUSION

2015 was an inflection year. The UN Global Goals, the Paris Agreement, and the US Senate legislation H.R.2262 reveal an irreversible awareness of *our space, our physical context*. We have now officially recognised our role and responsibility in taking good care of it on Earth and beyond.

The Space Value Optimisation tool supports the finance function in fulfilling its responsibilities in the age of responsible growth.

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ARMEN PAPAZIAN, PHD (CANTAB)

Armen Papazian is a financial economist with global experience in industry and academia. He is the founder and CEO of Finoptek, a fintech start-up developing a unique multi-tool, multi-instrument, cloud-based platform that introduces *Space Time Valuation* capabilities based on a proprietary model designed and created. His model introduces a new principle of value, Space Value of Money, into our current risk and time based paradigm. He describes his model, equations, and approach as Space Time Finance, and he is currently writing a book on the same, due to be published by Palgrave Macmillan in 2017.

He is a former managing director of Innovation and Development at Nasdaq Dubai (DIFX) where he led the launch of the Middle East's first structured products platform with Morgan Stanley, Deutsche Bank, and Merrill Lynch, the creation of the region's first tradable fixed income indices with HSBC, and the first fungible dual listing with a US exchange in the region.



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COMING NEXT IN THE REVIEW



In the next *Review of Financial Markets*, Daniel Broby, Chartered FCSI, will bring an experienced academic's hawk eye to bear on blockchain technologies in finance: solution or snake-oil? Daniel has enjoyed a successful career in both academia and practice, and is one of the Institute's longest-standing members. His research into financial benchmarks and markets has had important practical applications. Prior to his academic career, he worked in a number of senior executive positions in the fund management industry. These include chief executive, chief investment officer, and chief portfolio manager. Daniel's practical skill set includes financial modelling, accounting analytics, investment, index and portfolio construction.

He is now director of the Centre for Financial Regulation and Innovation at the University of Strathclyde, which in November was named Business School of the Year at the Times Higher Education awards. He is a regular host to CISI events.



5. $gEMP = g * EMP$ where g is a coefficient, like a, b, c, d , and e , in the NEW ASSETS equation, and EMP is employment expenditure.



Hitting the decks

MARTIN BADDER ACSI WEAVES THE WORLDS OF INVESTMENT MANAGEMENT AND DANCE MUSIC TOGETHER WITH HIS BAND SWINGERS, WHICH HAS PLAYED HEADLINE SLOTS AT NOTEWORTHY FESTIVALS WORLDWIDE

✦ LORA BENSON ✨ TOMSMITHPHOTOGRAPHY.CO.UK

You might not automatically connect the terms ‘deep house’, ‘tech house’ and ‘nu-disco’ with the world of investment management. But for Martin Badder ACSI, investment manager at Accrue Investment Management in Bath, this fusion is all in a day’s work as he indulges his love of DJing and music out of the office.

Martin plays keyboards in his own electro swing band called Swingers, now in its third year. The three-piece band plays DJ sets with live musicians, and has played headline slots at Glastonbury, Boomtown, international arts festival WOMAD and the Isle of Wight Festival in 2016, bringing a rock show attitude to the dance music scene with vintage remixes and glamorous onstage dancers. The band, which has been likened to Basement Jaxx, gives an extraordinary, energetic and charismatic performance: “Glastonbury was a highlight,” says Martin. “We had 10,000 people in the field watching us on the Saturday night; it was so much fun.”

But the biggest crowd Martin has played to is 120,000 in Phoenix Park, Dublin, when he was playing keyboards for Pina Kollars (Real World Records): “The noise from the crowd was unbelievably loud; it sounded like a jet engine!”

Martin has played in most European countries and further afield: “I played The Viper Room in California which is probably my favourite venue so far. Los Angeles seems to be so focused around music and fashion; it’s really an inspiring place to visit.”

Martin was born in Bath and educated at Corsham Comprehensive School. He can

trace his love of music back to watching a keyboard player on *Top of the Pops*, which led to him beginning piano lessons at the age of four. He started writing and producing electronic music as a teenager, signing his first major record deal with London Records at the age of 17. This was followed a few weeks later by a publishing deal with EMI.

“I was a keyboard player first, playing in my own bands and for other artists. I spent ten years touring the world playing keyboards with Countermine, my first band. We supported The Stone Roses, Ronnie Wood, Blondie, Simple Minds, The Charlatans and Bryan Adams.”

“We had 10,000 people watching us on the Saturday night; it was so much fun”

Martin’s financial services career began after his decade of touring, when the first record deal came to an end. He began as an account executive at Hoodless Brennan, now Beaufort Securities in Bristol. “The managing director gave me the challenge of acquiring 100 clients. After establishing my client base, I passed my exams within the first year.

“The DJing came later, and now gives me an opportunity to play my own tracks out. I was asked by a friend to fill in for him at a small club in Bath called The Common Room. Having never DJ’d before, I enthusiastically gave it a go. Sticking to 90s house club classics seemed to work and

formed a good starting point. Pretty soon I was DJing once a week or more.”

Now at Accrue Investment Management, Martin still looks after many of his original clients from the early days, while balancing his more conservative day job with regular dance floor gigs.

He says there is a lot of mileage in playing tracks that sample a recognisable vocal line: “This gives those on the dance floor something to latch on to. I get so much pleasure out of playing music to people, looking into the crowd and seeing smiles on everyone’s faces. This is the best thing in the world. It feels so good to be able to do this and is very addictive!”

When he is not out DJing, Martin is in the studio producing his own material. He refines these tunes on the dance floors of his regular nights before releasing them: “I have one track out so far in 2016 and have another two out in December 2016: ‘Mandem skank’ on Datatech and ‘Freak yeah’ out on Bunny Tiger.”

One of Martin’s main New Year resolutions is to teach his two-year-old son, Bodhi Blue, the piano, and when he is not playing his music he is a big fan of Crossfit, training six days a week, which gives him the energy to perform well both in the office and on stage.

➤ Contact lora.benson@cisi.org if you have a hobby you think will interest other CISI members. You will receive a £25 voucher as a ‘thank you’ if we publish your story.

The magic of pension planning for business owners and the need to act now

JULIUS LIPNER, FINANCIAL PLANNER AND INVESTMENT DIRECTOR AT CONSILIA WEALTH MANAGEMENT, EXPLAINS HOW A SMALL SELF-ADMINISTERED PENSION SCHEME CAN BE USED TO BUY YOUR OWN OFFICE AND SAVE FOR YOUR FUTURE

◆ JULIUS LIPNER

JULIUS LIPNER BIOGRAPHY

Julius is a financial planner at Consilia Wealth Management. He left Oxford with a Master's degree in Economics, gained the Chartered Financial Analyst credential and spent 15 years in the City. This gave him a wealth of experience in understanding people, businesses and investing money over several economic cycles.

As a financial planner and adviser, Julius brings his knowledge and far-reaching experience of the financial world to a deeply fulfilling role, helping and empowering people to take control of their personal finances. He champions spreading financial literacy in general and enjoys giving talks on the subject to audiences of all types.

CASE STUDY BRIEF

Thomas had been referred to me by an existing client. He is a serial entrepreneur and (reluctantly) thought he should have a financial health check in anticipation of becoming a father for the first time. He walked in to see us dreading it and aiming to leave after 30 minutes. He did not know exactly what he wanted, but after we listened carefully to him we were able to help him establish and meet several of his financial planning goals.

Thomas is an amazing client, in that his view of financial planning was revolutionised following our meeting to discuss what he perceived to be a boring topic: pensions. The buzz of bringing about this realisation in people is very rewarding – it's what keeps me in the game.

Thomas is a young, dynamic, highly entrepreneurial software developer who runs his own business. He left school at 18, tried university, decided it wasn't for him, so left to pursue his passion for computer programming instead – before Facebook and Twitter had shown how lucrative this could be. A classic serial entrepreneur, Thomas put his knack for programming to good use by setting up and selling several small programming and app-related businesses. By the time he came to see us, he was newly married with his first child on the way. On the recommendation of a mutual friend (and insistence of his wife), he thought he should see us for a “quick financial health check but nothing else” as long as the meeting “didn't last more than half an hour”. Challenge accepted.

NEW DIGS

It transpired that Thomas was looking for new office premises as he was fed up renting and living with the constant pressure of a landlord who could evict him at any moment if he didn't agree to an onerous rent rise. This led us to talk about pensions – a tricky segue, given that Thomas (in his own words) was “too cool for school, so discussing pensions is going to be a big ask”. However, once we showed him how he could use a small self-administered scheme (SSAS) to buy his

own office, he became enthusiastic. Owning an office was huge for him – he saw it giving him more peace of mind, stability for his business and freedom to plan properly for its future.

An SSAS is an occupational pension scheme that gives its members considerable flexibility and control over the investment policy and underlying assets. For example, you can own a commercial property through it and can have other members join, who are likely to be directors or key employees of a company (known as the ‘sponsoring employer’), and can club together to invest. As a pension it enjoys considerable tax benefits and it can even make a loan back to the directors of the sponsoring employer. This access to liquidity is important for company directors as they often fear putting money into a pension that locks it away forever.

Owning an office was huge for him – he saw it giving him more peace of mind

Owning your own offices through your pension is a great way for a business owner to save for their future, as when they eventually come to retire and sell up, the pension will continue to receive rent from the buyer of the business. Indeed, shortly before sale they can even rewrite the lease agreements between their firm and the office building to include upward only rent reviews – ongoing rental income provides a great source of inflation-linked income for old age. Also, rent payments (a corporate expense), running fees or additional

contributions into a pension by the company reduces its overall corporate tax rate, meaning more money can be saved by the business owner in the long run. Finally, as the pension is outside the entrepreneur's estate, assets inside it are sheltered from inheritance tax. All of this was music to Thomas's ears.

Boring old pensions helped Thomas to achieve several of his financial goals

This would also give Thomas a ring-fenced asset separate from his business. Many business owners think that their business is going to be their pension – but this isn't always the case. For one reason or another (often outside of their control), businesses fail. Having an asset such as an office building ring-fenced inside a pension is invaluable if the business ever goes bust as it's protected from creditors.

PREPARING EARLY

As the Autumn Statement was coming up, we started planning with a sense of urgency. With the Treasury seemingly unable to stop itself from tinkering with pension regulation, we had to act quickly to make sure we used all of Thomas's annual allowances, carry forward allowances and higher rate tax relief before anything changed. Being a high margin software

business, his company had amassed a large cash pile that we were able to move into an already existing pension. The beauty of an SSAS is that it can also gear up by 50%, so all this meant that Thomas could go and start looking for new premises right away.

Boring old pensions had now become a fantastic vehicle for Thomas to achieve several of his financial goals in one fell swoop – new offices, decent retirement income, accelerated savings, reduction in corporation tax, inheritance tax and the provision of a contingency plan in case his business ever failed. He was fascinated.

What was pleasing about this case was how one issue in a client's financial life opened up a whole nexus of other avenues to explore. The pension was simply the key to open Thomas's mind to what careful financial planning could do for him. Products are just a means to an end, and as a financial planner, if you focus on helping clients achieve their goals, everything else then falls into place. Our initial meeting blossomed into a series of other meetings focusing on his personal financial plan. This in turn helped him set definite financial goals for his firm as he now knew what he wanted to achieve and by when in his personal finances. Our initial meeting, which "definitely couldn't last more than 30 minutes", was still in full flow two hours later.

WHAT HAPPENED NEXT

We built a thorough financial plan for Thomas, working out goals and cashflow targets his business would need to achieve so that his personal financial planning goals could be met. We used his pension to buy offices, maximised his tax opportunities, set up savings vehicles and specific contributions to help him achieve his goal of financial independence.

We used the business to pay for protection policies for cross-shareholder agreements to secure the business in case anything happened to him. We also introduced him to an accountant who showed him how he could employ his wife and give her shares in the business to enhance their income. All this gave him significant peace of mind so that he could get on and do what he does best – build a business.

TAKEAWAYS:

- 1. Clients hate talking about products – they like talking about their goals. Products are there just to help them achieve these. Entrepreneurs (especially young ones) are usually focused on excitement, fast pace and opportunity – talking about financial planning or pensions is usually diametrically opposed to this unless you can directly link these to solving their problems.**
- 2. Timing is important – for example, be on the ball regarding pension legislation changes (which are currently moving quickly). Clients appreciate you calling them up if they can take advantage of something and this can be one of your useful touch points with them.**
- 3. Business owners have a wide array of levers to pull to save efficiently. Make sure you know them all and incorporate these into a comprehensive financial plan. It will deepen your relationship with them no end.**



Getty

SANDY ROBERTSON CFP™ CHARTERED FCSI, MANAGING DIRECTOR OF ACUMEN FINANCIAL PLANNING, TALKS ABOUT THE VALUE OF KEEPING FOCUSED ON A CLIENT'S DESTINATION WHILE ALSO ALLOWING FLEXIBILITY ALONG THE WAY

Giving clients lifelong security



**Sandy Robertson CFP™
Chartered FCSI**

Sandy, managing director of Acumen Financial Planning, has worked in banking, accounting and financial services for 40 years.

In 1995, he was the first person in Scotland to become a Fellow of the Institute of Financial Planning (IFP), now part of the CISI. Sandy is a member of the Institute of Bankers in Scotland, a Fellow of the Chartered Association of Certified Accountants, a CERTIFIED FINANCIAL PLANNER™ professional and a Chartered Fellow of the CISI.

He is trained in collaborative practice in accordance with the International Academy of Collaborative Professionals and helps develop standards on the financial matters involved in divorce and separation.

Acumen Financial Planning was formed in 2002 and has grown from a small team to an established firm, with some of the highest qualified planners in Scotland. Acumen Financial Planning is both accredited and chartered, and has offices in Aberdeen, Edinburgh, Elgin and Peterhead, with 35 staff currently serving 1,750 clients across the UK.

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Acumen Financial Planning won this year's Accredited Financial Planning Firm™ of the Year Award.

Why did you decide to enter?

We believe this is one of the most prestigious accolades for financial planning firms and it is something we have always aspired to. Having been highly commended the previous year, there was no question about entering again. We are very pleased and proud to have won this year.

When did you become an accredited firm? What has happened since?

We became accredited shortly after the IFP began accrediting firms in 2011. It was a culmination of events really. We had been approached by several firms to join forces with them and we had been thinking about whether we wanted to join, sell or continue alone. We decided that Acumen was not for sale and so we decided to future-proof the business by making sure we had the right people, processes and systems in place to be in as strong a position as we possibly could be to ensure excellent client service.

What has accredited firm status brought to your firm and why should others seek to become accredited firms?

It has added credibility for four groups: existing and prospective clients and existing and prospective members of our team. We feel that, as a result of being accredited, we are getting stronger candidates coming forward

when we advertise through print or social media, looking to strengthen our team.

What other accolades and awards has the firm picked up in recent times?

In the past we have won the New Model Adviser Scottish Planning Firm of the Year Award, and been highly commended in the Professional Adviser awards. We have also been category winners of the Money Management Financial Planner of the Year awards, but have only really focused on applying for awards on a regular basis in recent years, now we have the resources to put our name forward. We believe it is not only a mark of distinction to our clients but a great compliment to our talented and hard-working team.

What sort of business is Acumen Financial Planning and what services does it offer? What's your USP?

We are financial planners first and foremost. To us, financial planning is getting every one of our clients through life via a series of mini projects, each one going from A to B with complete financial security. At every step, we give an honest opinion on what needs to be done to get them safely to their destination, helping clients achieve their full financial promise. We offer a comprehensive range of investment, pension and financial modelling services to support and complement our core financial planning offering.

How did you get into financial planning?

When I was in my early 20s I worked in the investment department of a bank. I enjoyed it and it sparked a career-long interest in finances, the stock market and people. I became an accountant and ran my own practice. We would regularly see visiting independent financial advice firms who wanted to give advice to our clients, but we weren't particularly keen to let this happen and wanted to find a way to give that kind of advice in-house. Coincidentally, I attended an Association of Certified Accountants event and one of the speakers was David Norton, one of the early IFP members, past president, a chartered accountant himself and a leading financial planner.

One of the most rewarding parts of doing this for clients is the genuine gratitude

I was truly fortunate to have met him, and subsequently attended the IFP's next conference in Oxford, where I met some of the other leading lights, like Ian Shipway CFP™ Chartered FCSI, Robert Lockie CFP™ Chartered FCSI, Paul Etheridge CFP™ Chartered FCSI and Julie Lord CFP™ Chartered FCSI. I learned so much from these engaging professionals who gave generously of their time. I challenged myself to become one of them and design a business around the core concept of financial planning. I was inspired to sit the IFP's fellowship examination (prior to the CERTIFIED FINANCIAL PLANNER designation being available). In 1996, shortly after gaining IFP fellowship, I led the Scottish team in the then Team Challenge and we won that year's competition. That was such a fantastic and enlightening experience that I enjoyed immensely, working with three fellow professionals, all from Edinburgh, none of whom I had met before.

What's the best thing about being at a financial planning firm?

Having control over the future orientation of the business. We guide clients by presenting them with options to achieve their financial goals. We are Scottish



Collaborative Law trained and this means we are trained to avoid clients having fixed positions in life. So we uncover options and explore solutions but we build in the ability to pause at any given point, and review the options.

One of the most rewarding parts of doing this for clients is the genuine gratitude and appreciation we receive from them for doing this. We apply financial planning principles to our own business to ensure its success and ultimate succession to others in years to come.

Name one new thing you like at the CISI

The Integrity Matters test. I think it is a good thing to have to sit and is a mark of a true professional demonstrating they are doing the right thing. The code puts clients first. Regularly as planners we can feel conflicted in situations at work and I think this helps give us tools to manage that.

You were involved in Financial Planning Week this year. What did you think of it and what sorts of things did you do?

In addition to the national press and support of the initiative, we promoted our free surgeries through the local press and flyer distribution to potential new clients to help them understand what financial planning is. We love to support this initiative; financial planning is what we do and we want to play our part in helping members of the public

understand the potential benefits to them. At a client event we promoted Financial Planning Week to some of our existing clients, as they have been, and continue to be, our biggest source of referrals.

What does a typical day look like?

As part of our long-term vision for Acumen Financial Planning, I will be heading up the business support unit within the firm. This deals with everything that is not related directly to client work. To that end I am transitioning my clients over to my colleagues. This is a two-year process and so I have a mix of year one meetings where I am running the meetings with the designated planner, and some year two meetings where the designated planner runs the meetings and I sit in. My clients are being moved to five of our younger planners – all of the highest quality.

What are your key tips for other planners?

1. Don't take yourself too seriously! Clients need to be relaxed. If they are relaxed they will engage in the financial planning process.
2. Donate the meeting to the client. Have an agenda and structure but let the clients do the talking.
3. People buy people. Be authentic, be natural, and allow your sense of fun and humour to come through.



iStock

Creative accounting?

EDWARD AT IGNITIUS DISCOVERS THAT HE HAS BEEN PAYING INVOICES FROM HIS REGULAR SUBCONTRACT PARTNER FIRM THAT DO NOT REPRESENT THE ACTUAL SERVICES PROVIDED. WHAT SHOULD IGNITIUS DO?

Edward is the head of training at Ignitius, a large national business that sometimes employs subcontract training companies and individuals to deliver training on its behalf throughout the country. This training includes preparing students for work by making ‘educational visits’ to potential employers, during which the students are

accompanied by the trainer, thus giving rise to additional costs. Linda Parkinson, trading as Liberate, is one of their frequently used partner firms and has been delivering an ongoing programme to employees from a part of the country classified as a developing area, where government grants are available to firms providing skills-related training.

Liberate submits monthly invoices to Ignitius that are generally paid in a timely manner, normally having been approved by Francis, who holds the necessary authority. When Francis is not available, invoices are referred upwards to Edward for authorisation.

The system has been working satisfactorily for over a year until an occasion when both Francis and Edward are unavailable and Liberate's monthly invoice is handled by Lee. Lee has not been involved before and so is unsure how to react when, on returning from lunch, he finds a note on his desk indicating that a telephone call has been received from Liberate advising that they have made a mistake in the wording of their most recent invoice and that they will be submitting a replacement.

A GREY AREA

A few days later, Lee receives the replacement invoice from Liberate and, as he is looking at it, his telephone rings. The caller announces herself as Linda from Liberate. She thanks Lee for agreeing to help with the resubmission of the invoice and explains to him that the first invoice had included a reference to educational visits, which, she explains, are a bit of a grey area. Lee says he doesn't understand what she means, so Linda explains that

there has been some debate over whether the school visits should be classified as work-related training. Her partner had discussed this with the government agency responsible for the training grants, and was told that it "probably would be acceptable", but this hadn't been confirmed in writing.

Accordingly, Liberate wants the invoice to make no mention of the visits, in case that causes a delay in them obtaining the grant monies.

The first invoice had included a reference to educational visits, which are a bit of a grey area

Linda goes on to say that Liberate's fees for undertaking this work are based on the assumption that they will be able to claim the grant monies and that if they cannot do so, it will make the work uneconomical for them and they might have to reconsider whether they can continue the training on behalf of Ignitius. Lee is concerned at being told this, principally because it relates to matters in which he has had no involvement and he decides that he will raise the matter with Edward.

On hearing what Lee tells him, Edward's initial reaction is that it is a problem only for Liberate, which will have to live

with the consequences, but, on thinking about it a bit more, he realises that there are, in fact, a number of reasons why the position of Ignitius is not quite so simple. For example, now that Ignitius knows about the problem, if indeed it is a problem, should they try to resolve it, and if so, how?

Should they:

- A. Accept what they have been told without comment and amend the invoice as requested.
- B. Tell Liberate that they cannot be a party to any form of sharp practice and terminate their contract immediately.
- C. Accept that it is in their interests to try to resolve the situation with Liberate and encourage them to discuss the situation with the grant-awarding body.
- D. Report the matter directly to the grant-awarding body, including a calculation of the amount of money that they believe Liberate may have wrongly claimed.

What would you advise?

Visit cisi.org/creativeaccounting and let us know your favoured option. The results of the survey and the opinion of CISI will be published in the April print edition of *The Review*.

A CLEAN BREAK: THE VERDICT

Wiseacre financial planning firm is advised of the impending divorce of a wealthy couple who are clients: Paul and Janet. How might it respond to the implications of this in a bid to maintain the firm's income?

Readers were offered four choices:

- A.** Encourage Paul, who will probably be a better long-term proposition, to stay with Wiseacre while recommending that Janet be redirected to another well-regarded financial planner.
- B.** Recognising that Janet will be the party requiring more immediate care and attention, suggest that Wiseacre should offer its services to her.
- C.** Because of the impact that a loss of even half of these clients' business will have, they should do whatever they can to erect an effective 'Chinese wall'

in order to retain both Janet and Paul as clients.

D. Ben and Gary at Wiseacre must accept that they are likely to lose a significant level of income as a result of this news and should take steps immediately to recognise this. If part of this is dispensing with Ben's personal assistant, then that is a necessary step.

Nearly 90 members responded and there was an interesting split, with the majority polarised equally between C or D.

Many commented that in theory it would be ideal to create a Chinese wall; however, practically, this probably is not realistic in a firm of this size as you cannot forget the information you would have already seen. Perhaps a more realistic option would be the

second response, which is to recognise there would be an immediate drop in the business's income. It is interesting to see that many wish to keep Paul as the client but let Janet go, although, arguably, Janet may need the most help. Even today, there is an assumption that Paul will retain the larger share of the assets, although any divorce settlement may undermine that assumption.

So, what's important here is to put in place processes to deal appropriately with clients in such circumstances. Realistically, the fact that one in three marriages ends in divorce, and many second and subsequent marriages take place, leaves planners with an increasingly complicated area to think about. Being prepared is simply facing reality.



Ikony/Gary Walters

HMRC directly targets the facilitators of tax evasion

HMRC'S NEW CORPORATE OFFENCE IS A NEW WEAPON THAT WILL TARGET THOSE COMPANIES IT CONSIDERS HAVE BEEN HELPING TO FACILITATE TAX EVASION

ALI KAZIMI MCSI, MANAGING DIRECTOR, HANSUKE CONSULTING, AND ROB SMITH, SENIOR CONSULTANT, HANSUKE CONSULTING

HM Revenue & Customs (HMRC) has been effectively increasing the resource that they have available to target tax evasion and artificial avoidance schemes. They are being given the political backing required to help plug the 'tax gap' which was estimated at £36bn in 2014-15.

In order to persuade persons who may have undeclared funds held offshore, HMRC has run a series of voluntary disclosure facilities. These have provided a range of benefits to encourage disclosure. However, the end of the Liechtenstein Disclosure Facility in December 2015 brought an end to the guarantee of non-prosecution. With effect from April 2017, merely holding undeclared offshore income and gains will be a criminal offence.

HMRC has already received the first tranche of data under the UK's agreements with the Crown Dependencies and British Overseas Territories (CDOT), which was exchanged in September 2016. This includes information from the Channel

Islands, Isle of Man and the British Virgin Islands. In September 2017, HMRC will then receive the first batch of data under the Common Reporting Standard (CRS) which will cover 54 countries in the first year and a further 47 in 2018.

By 2018, most of the world's major financial centres will be covered by CRS. This will include a number of centres which have traditionally had very strong privacy laws, such as Austria, Israel and Singapore.

From April 2017, holding undeclared offshore income will be a criminal offence

Given that CDOT and CRS both drill down to the underlying individual 'controlling persons' of passive investment companies and trust structures, this information will finally enable HMRC to gain access to valuable information in relation to who is sitting behind, for example, BVI Trusts or passive Bermudan

companies. As both forms of agreements refer to an 'individual controlling person', merely placing a corporate entity within the ownership chain will not be sufficient to frustrate the aims.

The data that HMRC receives under the Automatic Exchange of Information (AEOI) agreements will be processed through its 'Connect' software. This is military-grade technology that maps this data and compares it with other information that HMRC receives from UK banks, credit card providers, auction houses, salary details and social media, among other information. The system will then highlight inconsistencies as cases for enquiry. Connect contains several billion records, which is more than is contained in the British Library. By 2011, it had brought in an estimated yield of £1.4bn, which has paid for its estimated cost of £45m many times over.

CORPORATE CRIMINAL OFFENCE

HMRC is utilising the processing power of Connect to support its targeting of the

companies it considers to have helped facilitate the abuse of the UK tax system. Legislation is now progressing through Parliament to introduce a corporate criminal offence of failure to have procedures in place to prevent the facilitation of tax evasion, whether against the UK or an overseas tax authority. It is anticipated that Royal Assent will be granted in the first half of 2017, with the powers commencing from 1 September 2017. This will help HMRC to target large organisations where they would not be able to prove that there was a 'controlling mind'.

For an offence against the UK Revenue, HMRC will need to demonstrate beyond reasonable doubt that:

- the individual has committed deliberate evasion of UK tax
- an employee or agent of the company helped to facilitate the evasion, and
- the company has failed to put procedures in place to prevent this.

HMRC does not actually have to secure a conviction against the first two levels. It merely has to prove to a court that these have occurred. Accordingly, evidence from an individual's disclosure under the Liechtenstein Disclosure Facility (which had a guarantee of non-prosecution) could be used to then take action against the companies which helped to facilitate the evasion.

Prosecution would almost certainly result in being barred from overseas markets

HMRC has already confirmed that it will seek to prosecute cases even if the company has no actual footprint in the UK. If the company does not attend court to defend itself, then there is provision in UK law for a trial in-absentia.

Prosecution would almost certainly result in the company being barred from other overseas markets, such as the US and elsewhere in the EU.

Linked to the UK offence, the powers will also enable the UK to prosecute instances where the corporate has helped to facilitate evasion of overseas tax. The entity involved must have a permanent establishment in

the UK (including a branch or subsidiary) and the overseas country must ask HMRC to prosecute on its behalf. However, this marks a major departure for how the UK treats tax evasion offences.

A defence against both offences is that the company has adequate procedures in place to prevent the facilitation. HMRC has already indicated that these can leverage off those procedures that firms will have developed to comply with their obligations under the Bribery Act. However, given the significant negative publicity that would arise from the launch of a prosecution, it is evident that a number of firms are already seeking to de-risk their business model.

Previously, HMRC has prosecuted by exception, concentrating on recovering missing yield. However, the new corporate offence, when combined with the strict liability offence for persons holding undeclared offshore income and gains, demonstrate a new willingness by HMRC to significantly increase the number of prosecutions. This is reinforced in the level of political and media pressure that is evidently being placed on HMRC, for example in relation to the relatively low number of prosecutions that arose from the bank data that was stolen from HSBC in Switzerland in 2010.

ENABLERS OF TAX AVOIDANCE

Separately, HMRC is also using the information it is receiving to target the companies it considers to have been enablers in the chain of tax avoidance schemes. The consultation on the proposals closed in September 2016, with the intention of introducing the penalties 2017.

The proposals were very widely drafted and could potentially bring firms that have provided bank accounts or other routine services within the scope. The onus will then be on companies to prove on the balance of probabilities that it would be reasonable that they could not have understood the underlying purpose behind the transaction.

While full details have yet to be confirmed, the consultation paper does indicate that penalties could be up to 100% of the total tax lost to HMRC through a defeated avoidance scheme. If a scheme has many members, the sums involved will probably be substantial.

It is evident that firms will need to reconsider the effectiveness of their anti-money laundering/'know your customer' controls to ensure that they can appreciate the purpose behind transactions or accounts. Staff training and awareness will also be absolutely critical.

TAKING THE LEAD

HMRC is investing significantly more than the private sector in technology that will enable it to track down not just individual tax evaders, but their advisers, financial institutions and other bodies that have helped them to facilitate this.

Penalties could be up to 100% of the total tax lost to HMRC

HMRC has already acquired significant information from voluntary disclosures from which they can identify the companies that have been providing the necessary advice and support. The significant amount of additional data that HMRC will be receiving under CDOT and CRS, together with a statutory requirement on individuals to correct returns that have omitted offshore income and gains, will only increase the information.

The political will exists to crack down and HMRC now has the technology to do so. The first shots in the latest war on tax evasion and avoidance are about to be fired. Companies will need to ensure that they can protect their reputation.

About the authors



Ali Kazimi MCSI is a senior tax adviser with over 25 years' financial services industry experience. He is the managing director at Hansuke. Prior to this he held successive leadership roles within Big Four firms, including head of international M&A tax for Deloitte Middle East and head of tax at Barclays Global Investors (now BlackRock).



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Teaching financial fundamentals

THE LOW LEVEL OF FINANCIAL LITERACY IS A CHALLENGE FOR THE UK AND MANY OTHER DEVELOPED COUNTRIES. IT'S A PROBLEM THAT SHOULD BE ADDRESSED AT AN EARLY AGE

◆ ANDREW DAVIS □ JOHANNA WARD



Chairing and taking part in discussions on pensions – and our seemingly endless attempts to fix Britain's creaking retirement system – have become a regular feature of my work over the past few years. This is hardly surprising. They are a topic of enormous interest these days, thanks to former Chancellor George Osborne's freedoms, auto-enrolment into workplace schemes, collapsing annuity rates and so on. There's never a shortage of things to talk about.

But one subject that seems to come up more and more regularly is our general lack of financial literacy and the role that the education system should play in addressing this widespread problem.

Many people seem baffled and bored by finance

In the past, I've tended to doubt whether trying to teach financial literacy in schools is likely to do much good. It's not that I don't think the knowledge is valuable; it's simply that I'm not sure how effectively it can be taught.

Many people seem both baffled and bored by most things to do with finance – how likely is it that a few hours of lessons will change their attitude or aptitude for a subject that feels

complicated, scary and dull? However, recently I've been prompted to think again.

First, a fascinating report on financial literacy across 30 advanced and developing countries, published in October by the Organisation for Economic Co-operation and Development (OECD), demonstrates very clearly the scale of the problem we face. The survey rated respondents from each country in three areas – financial knowledge, behaviour and attitudes, with a maximum possible score of 21.

The average among UK participants was 13.1. That compares with the average score across all 30 countries of 13.2, and the average across all OECD (developed) economies of 13.7. Financial literacy everywhere is pretty low but these findings suggest that Britain lags behind even the mediocre performance of most other advanced economies. It no longer feels good enough simply to shrug and bemoan the difficulty of teaching people to be more financially capable.

The second thing that got me thinking was a discussion I attended in Glasgow, at which Robert Wright, a professor of economics at Strathclyde University, talked about this research. Professor Wright has studied levels of financial literacy among schoolchildren and adults in the UK and

his account of the results is fascinating. His work focuses on three concepts that form the basis of financial literacy (and which also figure prominently in the OECD study): compounding, the difference between nominal and real returns, and diversification.

The most important factor in determining whether people achieve a decent level of financial understanding, he said, is the age at which they start receiving this type of education. His view is unequivocal: financial literacy should be taught in primary schools. By the time children are at secondary school, it is already becoming harder for them to absorb basic financial concepts if they are encountering these ideas for the first time; and teaching them to adults is unlikely to be successful, he said.

You can draw a gloomy conclusion from this – that there's not much we can do to help most working Britons become more financially capable – or you can take a more optimistic attitude and argue that important financial concepts need to be woven into the curriculum in every primary school.

I tend towards the latter view, particularly after recently finishing a wonderful book called *The Marshmallow Test* by Walter Mischel, an American

academic who has spent decades researching self-control in preschool children. The test in the book's title involves sitting a very young child in front of a marshmallow on a plate and telling them that if they can resist eating it for 20 minutes, they can have two marshmallows instead of one. Even at three and four, his subjects displayed very different levels of self-control and the ability to defer gratification.

Britain lags behind most other advanced economies

But two important findings shine through. First, those with better self-control in early childhood had higher incomes and career attainment several decades later. Second (and more importantly), very young children could learn coping strategies to help them meet the challenge and master their urge to eat the marshmallow immediately. Between them, these conversations and pieces of insight that I've come across over the past few months have convinced me that there are concrete things we can do to improve financial capability and that we need to get on and do them. In a system that now places so much risk and responsibility on the shoulders of individual savers, it would be almost criminal not to try.

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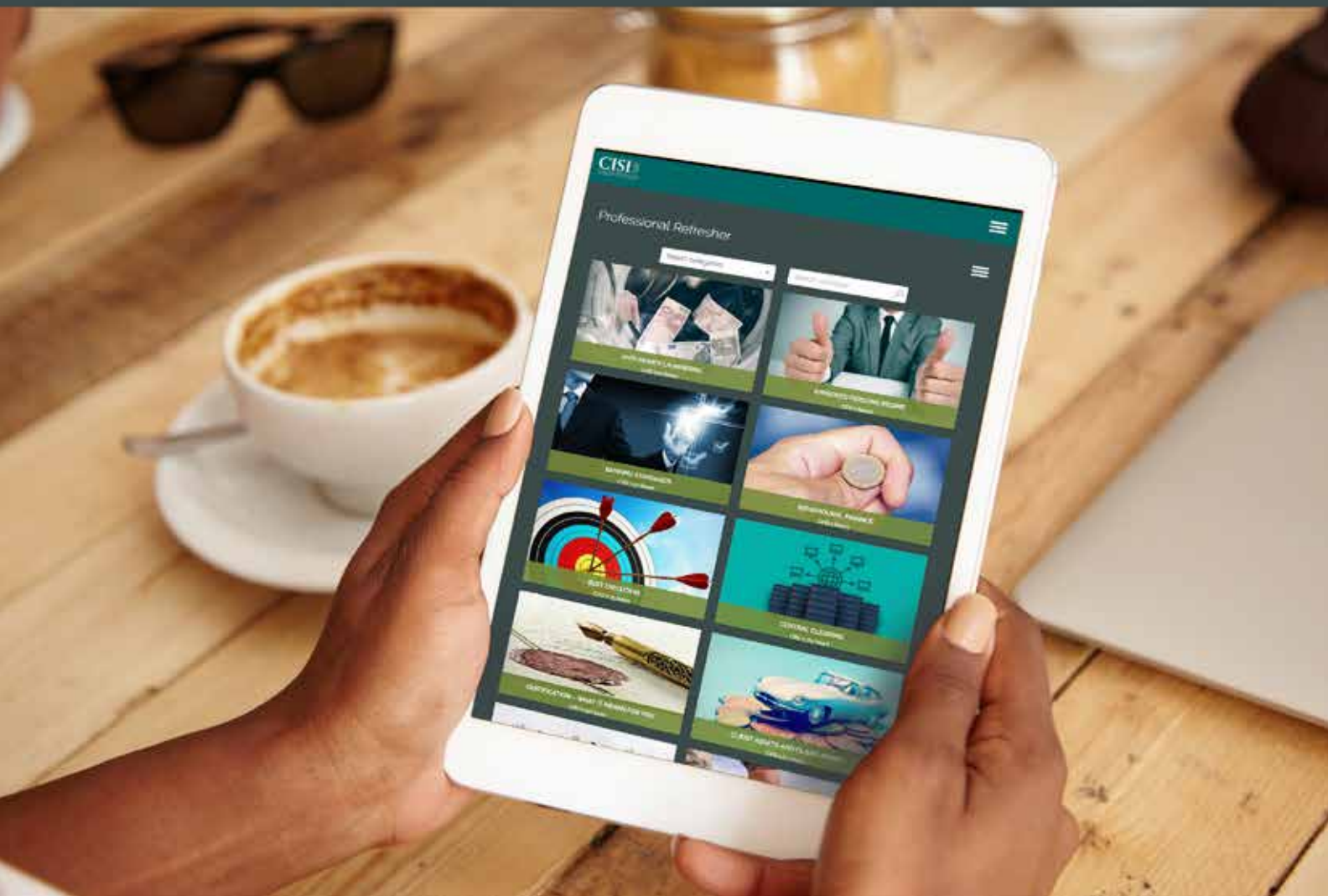
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We know that most of you are already undertaking and recording CPD with us annually. Our aim is to help our members demonstrate to consumers and the industry that they are committed to the highest standards of professionalism and integrity and that these standards are in place for perpetuity. We are phasing in these new CPD requirements gradually, over a two-year period, to ensure that we are allowing all our members time to get used to these new membership changes.

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