Financial Planning and Hybrid Advice Models

We have already dealt with a number of the proposals set out in the RDR Discussion paper in previous articles. One of the aims of the proposals is to remove conflicts or confusion that may be present in the current distribution model which may ultimately have an impact on the end user of a financial product. By ensuring that a customer is very clear about the type of financial advisor that they are engaging with, what they are able to offer as well as exactly what they are paying for, will allow customers to make informed choices.

The FSB has identified three broad activities which financial advisors do and for which they should be paid. Services direct to customers must be paid for by customers (which includes financial planning and product advice), activities which connect a customer and a product supplier should be paid for by the product supplier and services rendered directly to a product supplier, such as binder holder functions, must be paid for by a product supplier.

We will discuss here some of the proposals relating to financial planning as well as “hybrid” advice models.

FINANCIAL PLANNING

It is recognized that all financial advisors, irrespective of status (whether tied, multi-tied or independent) or the choice of products or product suppliers which they are able to offer, are able to provide objective financial planning or risk planning services. Under RDR, all types of financial advisors will be able to offer financial planning or risk planning as a service to their customers but the paper talks about setting out certain competence criteria and conduct standards that financial advisors will have to meet in order to offer this type of service to their customers.

Fit and proper standards will be set both in relation to the process of financial planning as well as the solutions which can be offered. The proposals also look to consider membership or qualifications provided by professional associations. The RDR paper indicates that the standards which are yet to be formulated may have reference to those standards already set by certain professional associations.

What will be important is that it is clear to customers what financial planning means, what qualifications or membership the financial planner has and what the financial plan will cover. Customers should also be able to understand what the objective or purpose of the financial plan is. This type of information will help customers to make informed choices and also to be clear about what they will receive in return for their payment for this service.

The proposals at this stage are fairly broad and while the framework is evident, the actual impact cannot be fully determined until the fit and proper criteria are known. As a starting point, financial advisors should think about the financial or risk planning activities which they do for their customers and identify the link with remuneration. It will be important that enough time is given to financial advisors who may not meet the set standards to enable them to obtain the requisite membership and/or qualification.

HYBRID ADVICE MODELS

One of the stated objectives of the FSB in RDR is to enable customers to be able to understand and compare offerings. As part of the introductory chapter of the RDR Paper, the FSB lists a number of what they describe as “more complex distribution models” (they list 8 examples). They also talk about “hybrid” distribution models, which in their description is often a combination or mixture of the more common relationships in the distribution space, e.g. tied, IFA, binder, etc.

Their concern lies with transparency, the potential conflicts and possible layers of costs that these hybrid more complex structures can introduce into the distribution of the products for customers.

Therefore, RDR seeks to remove noise, confusion or opaqueness from the system and ensure that there are no conflicting situations which could confuse or potentially prejudice customers. Under the current regulatory environment, many tied financial advisors are able to offer the products of another insurer. The RDR paper proposes that this presents a conflict and that disclosure alone is insufficient to reduce or remove the risks to customers.

It is, therefore, proposed that tied financial advisors only be allowed to offer the products of the insurer to whom they are tied and/or those products of any associated insurer or holding company. Financial advisors who decide that the tied model is most suitable to them will need to consider the impact of these proposals on their income streams as well as how a possible reduction in available product choice will impact their customers.

As a consequence of this, all advisors (from tied to IFA) will need to consider and decide what status (label, designation) they want to be, i.e. they will need to decide what relationship they wish to have in relation to product suppliers. Do they want to be tied or untied? (IFA or Multi-tied ito the proposals).

This also means they need to consider what they currently have vs what they will have or will be able to have or do under RDR, e.g. If advisors are currently tied advisors, what do they currently have and what will (in terms of the RDR proposals) they be allowed to have or do. Only then, will they be able to make a conscious decision of what or how their business should look.

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