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Many financial advisers are now considering how platforms can be used at the core of their business to improve efficiency, profitability and the service on offer to their clients. But how will this work in practice, given the current regulatory environment?

platforms and independence



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Ian Thomas considers how platforms can help advisers to maximise business efficiency without compromising their independence.

The concept of independent financial advice dates back to polarisation, which was introduced in the mid-1980s and was defined by an adviser's ability to select any product from any provider in the marketplace. Although we have moved beyond 'best advice' to 'suitable advice', most suitability letters, because of the regulations, still place great emphasis on the product aspect of the recommendation.

The Sandler Report in 2002 criticised the structure of the retail savings industry in the UK. Amongst its

observations was that product and commission complexity had not benefited clients. He argued for less complexity, better personal finance education and a greater focus on asset allocation in the advice process.

Some of these themes are now being developed in the FSA's Retail Distribution Review, announced in June this year, and have also been discussed in several high-profile speeches from senior FSA figures.

Callum McCarthy, Chairman of the FSA, recently set the tone by stating that the

status quo does not benefit clients, but also is not in the interests of providers or advisers. He claimed that 'the present distribution system is distinguished by a focus on business volume rather than quality' and that commission incentives, as structured now, do 'little to encourage (and may discourage) the fair treatment of customers'. He also said that 'the present system, with its in-built encouragement to churn and its product and provider bias, is not one which is naturally robust to claims for mis-selling, and the associated compensation liabilities'.

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a platform solution

So what can be done to improve the overall situation? Clive Briault, Managing Director, Retail Markets at the FSA, said in November 2006 'that it should not be the job of a regulator to dictate business models or market solutions. But we are clear that... the market needs to operate more effectively, and that it is right for us to be one of the catalysts for achieving this.' In another recent FSA speech from Dan Waters, the regulator began to encourage the use of platforms; he said: 'we have seen some very positive examples... of firms thinking carefully about whether and how they want to incorporate platform services into their businesses, in order to offer the best possible services to their customers that they can. I want those examples to become the norm.'

remaining independent

From the FSA's thematic research in June this year, we know that if a platform provides a solution to 80% of an adviser's clients, then those clients could all be transacted through the wrap platform. In this scenario, the adviser remains 'independent', provided that:

- the recommendation is suitable to the client's circumstances
- the adviser has considered products from across the whole market (whether platform-based or not)
- following de-polarisation, the client is given the option to pay by a fee.

Just last month, Katherine King, an FSA spokesperson provided even more clarification that the concept of

independence is moving on. She said: 'We previously had a reporting requirement which required [advisers to] report where there was exposure greater than 20% on one particular product provider. We certainly don't have a 20% reporting rule now... it doesn't matter whether you go for one or several wraps as long as it is right for your client.'*

summary

The FSA is looking at the overall structure of retail financial services, and at how to react to the rise of platforms in particular. Their statements so far support the general move towards principles-based regulation such as TCF, rather than prescriptive, product-focused rules.

It is now clear that platforms are not inconsistent with the concept of independence. An adviser works on behalf of, and in the best interests of, his clients. If a platform no longer represents good value then he has the option, or indeed the obligation, to select another firm to provide a similar service. Crucially, however, an adviser does not demonstrate independence simply through the use of many different companies' products and services.

Despite this, more specific guidance on the use of platforms would be welcome and we await possible future announcements in this area next year as a result of the FSA's distribution review. In the meantime, the current regulatory environment is supportive of the use of platforms and we can expect their usage to grow as advisers continue to benefit from the business efficiencies they deliver.

The FSA does still have some concerns about the use of wraps, which can be summarised as follows:

The transparency of platform charges

Clients need to understand what they are being charged. The project, looking at the 'best of breed' Skandia MultiFUNDS/Selestia platform to be launched in summer 2007, will ensure that the charges are both clear and consistent for our platform products. The principle will be that charges are for an adviser and client to agree at an overall portfolio level; the platform just administers the agreement by deducting units from the relevant product wrappers to pay the initial and ongoing fees/commissions.

The level of platform charges and suitability for a client's circumstances

If, for example, a client has very straightforward needs, then a very simple product would - other things being equal - normally be selected by an adviser. The FSA is simply re-stating that advisers must not lose sight of the client's interests, ie they shouldn't be offered a platform's products and services as a 'default' just to suit the adviser's business model if they are not needed.

That charges are commensurate with the service offered by advisers

Platforms typically offer a scaleable service which allows a more comprehensive 'wealth management' service to be offered to many clients. They also often allow flexible levels of trail commission, for example, to be paid to support this service. The FSA's concern is that advisers consider Treating Customers Fairly (TCF) principles when they are balancing their remuneration against the benefit the client is receiving.

* It should be noted that such exposure can still be monitored via Product Sales Data (PSD) returns.

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