Depolarization

WELCOME ADVICE

The impact of depolarization has been limited so far, but Keith Carby believes that good advisers still have a bright future – whichever way they move.

In 1995, a City University Business School research report took 271 pages to discuss "the key to success and survival in the insurance industry".[1] Whilst wide ranging in scope, there was not a single mention of the "R-word".

Whether or not such an omission was justified after the first ten years of regulation, very few of today's independent financial advisers (IFAs) would feel it was credible to ignore the subject in any analysis of the current picture after a second decade of living with regulation – and nearly four years with the new "super-regulator", the Financial Services Authority (FSA). For many advisers, "risk" (which they would see as having been inflated by regulation) has become the number two preoccupation – just behind the challenge of continuing to make a living by providing a good service to their clients.

That is not to say most IFAs feel negatively towards regulation in general or the FSA in particular. In my experience, by and large, they don't. Most accept that regulation was inevitable and that, undoubtedly, there have been positive consequences. Perhaps the adviser community ought to be given more credit for taking this pragmatic stance, given that their numbers have been savagely reduced, partly as a direct result, and the working lives of those that remain made even more demanding.

Critical concerns

Adviser criticism of regulation invariably relates to specifics, which are usually connected to one of three issues – perceived unfairness, irrelevance, or bureaucracy. In the limited space available here, I will discuss these concerns in relation to just one current topic – depolarization.

Had I been writing these words a year ago, it would undoubtedly have seemed a much bigger issue. But just now, four months after "D-day"[2], and after – or perhaps despite – the millions of words written about it and the goodness-knows-how-many man-years of effort analysing and planning for it, depolarization is seen by most IFAs as a non-event.

Thus far, depolarization has been commended to IFAs by its proponents on the basis of, firstly, greater reward for the same amount of work and, secondly, ease of administration. Neither benefit is currently perceived by most IFAs to be of sufficient appeal to warrant making a change – full independent status is more highly-valued than ever by the majority.

Yet a survey of financial services companies by the Grant Thornton Finance Market Group published last month concluded that:

> Despite the fact that overall consumer choice is predicted to increase, further analysis suggests that this will only be the case among banks and building societies as the move towards "multi-tie" partnerships by these organizations demonstrates. There are, however, indicators that the rest of the market will have to contend with company closures, particularly among IFAs.

How come?

Most IFAs can see why the banks and building societies believe that they will benefit. This is not a surprise given that, allegedly, they were one of the forces that brought about depolarization. In passing, it is perhaps more surprising – and a sign of modern commercial and societal realities – that the lobbying for this change on the grounds of "greater consumer choice" was so ready accepted.

But are the respondents in the Grant Thornton survey right about the effects of depolarization on IFAs? To assess this, it is necessary to look at how IFAs were already reacting to market changes.

In the face of reduced commissions and higher costs, IFAs reacted like all sensible business people would. Firstly, some have become more focused and have gone upscale. They have refined their propositions and placed themselves in a context in which they are doing high added-value work for clients, who need and value and can meet the cost of such services. IFAs in this camp have tended to place more value on the packaged approach to support, and are, therefore, more likely to be found in national companies or networks, since they believe this allows them to spend more time on what, for them, is the crucial task of finding more of these upscale clients.

Other IFAs have taken a very different approach to the same economic pressures. They have judged that it would be difficult for them to re-engineer their existing client banks, and have therefore had to place more emphasis on reducing costs. Consequently, their ways of working have not changed as much as for the first category of IFA, but they have grown even more self-sufficient and will invariably now be directly-authorized.

Other considerations

A complicating factor in this (admittedly over-simplified) analysis is "risk". IFAs in the nationals and the networks see themselves as being less at risk, albeit at the expense of a tighter regulating régime. Directly-authorized IFAs are at greater risk, in part because they (usually) have a less-rigorous compliance environment. So these perceived risk factors also affected choices.

Right now, neither of these IFA stereotypes is excited about multi-ties. The first group sees independence as crucial to its commercial strategy, since its route to the future is mostly high added-value to the wealthier client. The second might not view multi-ties as being incompatible with its marketing strategy as such, but for the moment the extra reward on offer appears insufficient to offset the value it sees in being free to operate in any way it chooses.

Perceptions amongst IFAs about multi-ties will be changed by the powerful forces in favour of depolarization. Already, new benefits for multi-tie business have been launched, including "buy outs" or "defined exits". Multi-ties are also being championed on the basis that they can represent part of the solution to the challenge of producing the next generation of IFAs. If these and other benefits are realized, then it will affect most of the IFA community – albeit differently.

The two groups of IFAs that I have described are not really mutually-exclusive but, rather, stereotypes taken from the extreme ends of a continuum. Most IFAs are in practice hybrids of the two categories. They have some clients who want and can afford a high-added-value service, but others (usually the majority) who don't or can't. And some clients may want one service for some things and the other for others. Like water flowing downhill, the multi-tie proposition will find its way to those clients that it suits – as judged by the adviser. For IFAs for whom the flow proves strong, then the move to multi-ties will happen more readily. For others, it will not affect the commitment to independence.

Where IFAs can find compliant ways of staying independent but gaining access to a multi-tie for the relevant client, they will do so. A minority only are likely to be converted fully to multi-ties, but their conversion will confirm the prediction of the Grant Thornton survey.

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Depolarization should be given its chance. The country needs more advisers, and if the only way to build the number is through multi-ties, then this has to be developed. If depolarization also provides a way for some IFAs to achieve a better living standard, then that is also to be welcomed.

Whilst it is regrettable to see yet another change that is likely to have the long-term effect of further attrition of the IFA community, there is some good news. For those who remain independent, it is now certain that they will enjoy a much higher status and will be seen as valued professionals. Earning a living as an IFA in the future will automatically mean the adviser is capable of providing a high-quality service.

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The fundamental restructuring of the sector has a few more years to run before this latest cycle is complete. It has been hard for most, and commercially terminal for many. The good news though is that, at the end of it all, Britain will have an IFA community that is the envy of the world. Those IFAs that survive will thoroughly deserve their place in the sun. ☐

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[1] *Effective distribution* by Peter Whitaker.

[2] 1 June 2005 in this case, rather than 6 June 1944!