

LifeSearch: Submission to the Thoresen Review of Generic Financial Advice

April 2007

Overview

1. Our general view on the Thoresen Review

LifeSearch welcomes the formation of the Thoresen Review to consider the development of a national generic financial advice network. We also welcome the review's priority status within Government. As Otto Thoresen stated at a recent conference, hosted by the Resolution Foundation, the current policy debate is not centred on *if* such a national resource is developed, but on *when* that resource can be developed.

Overall, we see the Government's stated policy objective - the creation of a national generic financial advice (GFA) resource - as a ringing endorsement of the valuable role currently undertaken by everyone who works in the advice chain. As one of the UK's leading financial advisors we appreciate the Government's acknowledgement of the value added by advice in the financial decision making process. Financial products are often complicated and faced with new challenges, such as the introduction of Personal Accounts in 2012, it is clear that consumers require wider access to information and advice.

We look forward to working with the review team in developing thinking on some of the key points of delivery.

2. About LifeSearch

AO 1 asks what advice service is our organisation responsible for delivering

LifeSearch is an independent financial adviser specialising in pure protection. Originally LifeSearch was set up as a non-advising firm but we realised in 1998 that we were doing customers a grave disservice by selling them what they wanted as opposed to trying to help them towards what they needed. This is why we changed to the advisory model, which we felt would fundamentally better serve the interests of customers.

AO 2 asks how our advice is delivered and AO 4 asks how it is funded

The aim of LifeSearch is to bring advice on protection to the mass market. We do this by offering financial advice over the telephone, allowing more people to get access to specialist advice at a lower cost than would be possible with face-to-face advice. This allows LifeSearch to compete with non-advisers who compete primarily on price and who, thanks to lighter regulatory requirements, have much a lower cost of doing business than advisers. Earlier in the year the supermarket retailer ASDA signed a pioneering deal with LifeSearch to handle its life insurance sales *on an advised basis*, which is unique development within the sector. It also provides the means for up-scaling the LifeSearch advice model to over 14 million UK adults.

This service is funded through customers who typically pay an upfront commission. Our remuneration model is universally adopted throughout the protection market reflecting the fact that consumers are generally unwilling to pay a fee-based arrangement for advice on general insurance products and also because many, though not all, products sold in the protection market will require point of sale underwriting which can be a lengthy and complicated process taking several weeks or some cases longer. This means that the advisor will typically be required to undertake a lot of the activity on behalf of the client at the outset of the sales process.

AO 3 asks about our legal and governance structure

As a regulated financial advisor LifeSearch is authorised and regulated by the Financial Services Authority (FSA). As such we are subject to the prudential and conduct of business rules as defined under the Financial Services and Markets Act 2000. All our sales advice is governed by statutory requirements contained in the Insurance Mediation Directive (and other legislation) which forms the basis of the FSA's Insurance Conduct of Business Handbook, which was introduced in January 2005.

AO 5 asks how we identify our customers and their needs

Customers are identified through a number of lead generators. The Internet is becoming an increasingly important channel owing to the array of popular search engines, such as Google or Ask, which enable consumers to readily find contact details on a range of providers. Our website acts as a 'shop window' which can give the customer access to information about the products on offer before directing potential clients to a telephone-based advisor. This shop window is particularly effective in reaching certain market segmentations such as younger consumers who are generally more computer savvy. In addition to this, we receive referrals from existing customers as well as through introducers such as ASDA.

As a regulated advisor we are bound by the FSA's *Know Your Customer* (KYC) requirements to ascertain the consumer's financial circumstances and produce a statement of their wants and needs detailing what our recommendation to that customer is and on what basis we have reached that judgement in line with the suitability requirement. This suitability test ensures that the client always receives the most suitable product to fit their personal circumstances. The advent of principles-based regulation in the form of Treating Customers Fairly (TCF) also requires firms to adopt more client-centric approaches to meeting the needs and expectations of consumers. At LifeSearch we take TCF very seriously and have developed a full range of TCF policies to help ensure that our organisation better serves the needs of customers at each life stage of the product.

Specific Issues for Policymakers

3. Defining advice

AS 3 asks what is the most appropriate way of describing "generic financial advice" provision

The call for evidence highlights 'generic financial advice' as purely a working definition. It is a definition which currently causes us some concerns. At present the 'advice chain' is very diverse, incorporating both the private sector and the third sector. However, within that diversity the parameters for advice are clearly defined with providers performing a variety of services in large part driven by the constraints placed upon them by financial regulation. This includes the unregulated benefit and debt advice services provided through national advice help lines and local advice centres, through to fully regulated financial advisors offering 'personal recommendations' on financial products. In light of current approaches there are immediate difficulties with the term 'generic financial advice' if that is defined to mean advice that is not

regulated, even if that advice is highly specific and personalised. We feel that this undermines the clear demarcation between regulated advice on the one hand and unregulated information on the other. FSA research conducted as part of the ICOB review demonstrates that some consumers already struggle to understand that demarcation. There are already enough non-advisors in the market place masquerading as advisors, which undermines consumers' ability to differentiate between distribution channels on an informed basis. It is this trend which has caused the FSA to consider stronger status disclosure for all oral communications in the light of poor market practice by PPI sellers. This confusion about the status of non-advisors could be exacerbated with the introduction of a GFA service. If it is to be unregulated, it must not be called advice.

We believe that with greater consumer awareness the current boundary could and should serve consumers well in helping to clarify their rights and responsibilities against those of the advisor. The decision for policymakers involved in devising the generic advice model is not whether to redraw the current boundaries but to determine simply which side of the boundary the generic model should sit and then decide on an appropriate name. This will help determine just how far the GFA model can go before handing over to the regulated advice market.

4. The handover from generic to regulated advice

BS 7 asks where people should be referred to after receiving generic financial advice and whether it should be possible to refer people to a commercial provider

At present the different outlets for advice do not overlap as well as they could. Typically, the handover from current generic advice providers to the financial services industry will involve referring the client to an organisation such as IFA Promotion who will provide the client with details of local Independent Financial Advisors (IFAs). This approach consists of both good and bad elements. On the down side, the quality and specialisms of IFAs can vary quite markedly and the generic advisor has no means of ensuring quality control over which IFA is finally selected.

On the plus side, whichever advisor is selected the client is protected against poor recommendations by the "suitability" requirements placed on the advisor. It is for this reason that ALL referrals under the new system should continue to involve an 'independent' regulated source of advice as the handover point ("the first port of call") rather than referring clients direct to commercial providers, who may not actually be in the business of providing any advice but simply selling their own products.

From this perspective it is not clear on what sound basis the GFA model could refer clients to commercial providers. For example, how would it select which particular providers or products are appropriate or suitable? We believe that this is the job of the regulated advisor who already takes those decisions based on what is in the client's best interests.

5. Ensuring effective Delivery: telephone trumps all other means

BS 3 asks what are the best ways to reach the target market (i.e. the most vulnerable to the consequences of poor decision-making)

Given the important handover role of the IFA, combined with current capacity constraints within regulated advice market, it is clear that IFAs themselves need to be at the forefront in developing cost-effective and accessible means of delivery which can better compliment the GFA model. While the delivery mechanism will need to consist of a mix of communications channels, in order to suit the needs of as many users as possible, (rather than a "one-size-fits-all" approach) it is nonetheless true that most information will be delivered through one major channel.

While web-based communications are by far the most cost-effective in terms of potential volume, they are also the least effective in terms of potential outcomes. This point was reflected in the findings of the Resolution Foundation's consultation during 2006.

We feel that the value in developing a generic advice resource is that it is responsive (in 'real time') to the needs of the user-group, which means that it should be based to as great an extent as is possible, on oral communications. This consumer preference for dealing with a human being was made clear in FSA research to market test the effectiveness of Stakeholder decision trees. We therefore welcome the call for evidence in highlighting the need for a telephone-based point of contact. In exploring the "potential for additional face-to-face services" these will clearly be welcomed if economically viable, though they will of course be more costly as the likely volume of cases handled per advisor will be much less than compared with phone-based services.

Our experience as a telephone-based advice provider (with a sister company offering face-to-face advice) is that the time and cost efficiencies of telephone-based methods of communication are clear, particularly in extending market reach to financially excluded groups. Whereas we typically provide advice to 30 clients per day on a face-to-face basis with 13 advisers in the field (a ratio of 2.3 clients per advisor) this increases to around 800 clients per day on a telephone-basis using 54 advisers (a ratio of 14.8 clients per advisor).

These efficiencies enable additional benefits in helping to meet social inclusion objectives as a direct result of using a phone-based approach. It cuts out travel costs - which may be an obstacle to those potential users who are on lower incomes or who lack access to a car - and it can be accessed easily from within the users own home (which will particularly benefit those with mobility problems, such as the elderly or disabled, and those undertaking domestic caring responsibilities who might not find it easy or convenient to access such services) as well as from mobile phones, which have high penetration across all income groups.

These benefits are reflected in LifeSearch's own consumer base in which our own telephone-based model means that those on lower incomes are well represented. Perhaps one of the most powerful statistics we can provide - given the popular assumption that financial advice has largely deserted the mass market - is that we can provide affordable regulated financial advice in which the typical LifeSearch customer is earning at- or below the average household income level. This is clearly the same target audience as the Thoresen Review.

This overlap is likely to be furthered following our recent strategic partnership with supermarket ASDA. As a major retailer ASDA has around 14 million UK adults amongst its customer base. This comprises of mostly social group C2s and Ds. As of February 2007, all of ASDA's life insurance products will be sold with financial advice - via LifeSearch advised centres - marking a major return of 'financial advice on the high street'. This is critical from our perspective as it will for the first time make our approach to distribution scaleable to the mass market.

We believe that our business model provides perhaps the closest model in the private sector to that envisaged by the Thoresen Review. The characteristics of our service are as follows;

- Based on providing cost-effective advice over the telephone;
- Supported through web-based information;
- Provides advice nationally (there are no geographical barriers to access);
- Self-financing (funded by the user) and therefore sustainable; and
- It is not exclusive to any one group and easily accessible to people who have been hitherto overlooked by 'mass affluent' or 'high net worth' financial advisors

6. Consumer engagement

DS 4 asks whether there is evidence on which engagement mechanisms work best overall. The call for evidence also states that a lack of access to financial advice can lead to poor financial decisions and the need for crisis intervention. "A more preventative approach" based on advice is

seen as the way forward. While we do support this approach, access needs to be followed through with effective consumer engagement. The consumer has to feel that they have a need to act long before a crisis invention is too late. This issue of engagement is one that all parts of the advice chain find challenging.

At present, most clients using advice centres have already run into financial difficulties, typically with mounting debt problems. In this case the 'crisis' is the prompt to act. For regulated advisors the prompt comes at an earlier stage, such as an important life event such as becoming a home owner or starting a family. While this is a more proactive consumer response it is not universal. Industry figures reveal that there huge gaps in personal provision of protection, savings and pensions.

The challenge, therefore, is to raise consumer awareness and encourage greater proactivity. As part of our partnership deal with ASDA we are currently piloting a range of different approaches to in-store delivery mechanisms and different approaches to consumer engagement. This may extend to in-store face-to-face advice. The tie-up with ASDA is still in an early phase - such a project to provide financial advice through a mass market non-financial retail brand has never been attempted before now - though it demonstrates how quickly the environment for regulated advice is changing. Once we have more detail on how our own trails in mass market engagement are working we would be happy to share detailed results with policymakers.

7. Responsible product design

Another important angle where change is occurring is in the field of product design. This has probably received less attention within the generic advice debate than is merited, given that simplified products will simplify the choices consumers are faced with. This will not only make the lives of consumers easier but will also help advisors - both regulated and generic - to provide clearer advice that consumers can more readily understand and act upon with confidence.

To some extent the Government has taken on the mantle of product design in the pensions arena through its bold proposals for Personal Accounts which will provide a simple pension product, offering limited fund choice. This builds on previous forays into product design such as Stakeholder, Child Trust Funds and 'CAT' marked products. While previous reforms enjoyed only limited success, clearly more needs to be done to simplify consumer choices. The market for protection insurance and long-term investments remains largely confusing for consumers purchasing without advice. As such, providing good quality advice on these aspects of financial planning will provide a major challenge for generic advisors.

LifeSearch, in partnership with a major insurer is taking steps to address this in the protection market with a new product - *Real Life Cover* - which combines the essential elements of household protection into one product. The Thoresen Review should give due regard to this development, and to the contribution made by product innovation and simplification more broadly, in helping a generic advice model to succeed.

8. Options for funding; addressing the cost of delivery

CS 1 asks to what extent generic advice should be free at the point of delivery while CS 2 asks whether there is any evidence that supports a commercial case for a generic advice service. While generic advice is seen as the means of filling the 'affordable' advice gap, the questions raised in CS 1-5 illustrate that it is not yet clear how, or who, will share in the burden of meeting the costs of supplying it.

Indirect funding models

This could consist of subsidy through general taxation or possibly through contributions from industry. While the upfront cost to consumers could be reduced or eliminated through a special levy on FSA authorised firms, or by simply increasing the existing FSA levy, it is important to recognise that these costs will be passed on to consumers who will still be paying for the GFA service only they will do so through paying higher prices for the financial products they eventually buy. The distributional effect will mean people buying products are subsidising those who don't. Effectively 'hiding' the true cost of the GFA delivery in this way could have unintended and disastrous consequences on regulated advice, particularly in light of the current debate around commissions versus fee arrangements as part of the FSA's retail distribution review. If that review should lead to the introduction of factory gate pricing where regulated advisors are expected to itemise the cost of delivering their service, while potentially competing with a GFA model which is perceived in the consumer's mind to be 'free' then it would not be difficult to foresee that many consumers will potentially choose GFA over regulated advice on grounds of cost alone - irrespective of whether they can afford regulated advice or whether regulated advice actually offers a more comprehensive service.

Self-financing

Alternatively the GFA could raise revenues to fund or part-fund its own activities such as levying a small charge for users or selling advertising space on its website. In our experience as a regulated financial advisor we find that consumers who earn low incomes are prepared to pay for

advice where it is deemed to be affordable. The problem is not so much that consumers are unwilling to pay but that there is insufficient availability of affordable advice.

Creating a pricing structure based on nil-cost to the end-user will potentially undermine all forms of existing regulated and non-regulated advice by creating uncompetitive downward pressure on pricing across the whole advice sector. While many third-sector providers currently operate on a voluntary basis, a nil-cost GFA model would effectively deny them the opportunity to explore at a future date how they can adopt pricing models.

Undermining existing advice on price would not only prove detrimental to the sustainability of existing advisers but it would also be negative for the GFA service, as regulated advisers (and indeed other existing sources of advice) present the best means of limiting the cost burdens on the new system of generic advice. The presence of affordable and easily accessible financial advice will enable consumers to switch more easily from generic to regulated advice. In this respect, affordable regulated financial advice can provide a partial solution to the GFA's cost issues by reducing its case load. The pricing structure for GFA should reflect this complementary role otherwise the GFA model could run the risk of substituting rather than adding to existing provision.

9. Addressing the issue of accountability; who is liable for poor decision-making?

BS 9 asks what are the legal implications of giving generic financial advice, BO 8 asks how we deal with questions of liability for inappropriate advice while BS 10 asks what would the creation of a new generic financial advice service materially affect advice providers.

These questions can be answered by clearly defining what the limits of GFA would be, and by reference to our FSA obligations. In attempting to give a working definition of generic advice (in p.3 of the call for evidence) the Thoresen Review team is clearly aware of the regulatory distinctions between 'advice' involving personal recommendations on the one hand versus 'information' on the other. This distinction has important implications for consumers in how advice is regulated.

Owing to issues of accountability in the distribution chain (and where to apportion any liabilities arising from poor financial decision-making) BS 9 raises an important point and one which was raised at the recent Resolution Foundation conference. Generally, we do not feel that it is desirable for consumers to substitute regulated financial advice (wherever it is an affordable option) for generic financial advice as if the two were inter-changeable, nor is it acceptable to blur

the distinctions between the two in the minds of consumers. The legal right to make personal recommendations about specific products and providers must remain the preserve of the regulated financial advisor. While GFA can provide personalised information as part of its approach this must limit itself to providing the contextual overview of an individual's financial planning needs with clear parameters in place to ensure effective handover to a trusted and independent source of regulated financial advice takes place at the appropriate time.

Under the current FSMA regime regulated financial advice offers consumers important protection against the sale of unsuitable products. This "suitability" test means that the liability for poor sales rests with the advisor not the consumer. In non-advised sales, where the less stringent "appropriateness" test applies, it is the consumer who is liable for ensuring that a sale is suitable to their needs. This limits their access to the Financial Ombudsman's Service (FOS) and with it access to possible compensation. As financial advisors already accept liability for consumer decisions and are required by regulation to ensure that they carry adequate indemnity against possible future consumer complaint. It is unlikely that any GFA 'adviser' would ever be prepared to accept the same degree of responsibility.

By limiting the functional scope of GFA not to include personal recommendations or accept any liability for consumer decision-making, this should help to limit any legal implications for GFA 'advisers' as well as helping to reduce the material affect on existing regulated advisers.

However, the overarching need to keep any legal liabilities on the GFA 'adviser' to a minimum, by ensuring that the role of regulated advice is clearly distinct from the GFA for legal purposes, will of course have implications for consumers. Depending on how this issue of liability is addressed vis-à-vis the operation of the GFA service, we feel it would be potentially inequitable to expect those on lower incomes to make important long-term financial decisions based *purely* on generic advice, however much it may be personalised, if that were to lead to those people accepting fully liable for their decisions and, as a consequence, enjoying only partial access to the FOS.

We believe that the easiest way to provide consumers with adequate legal protections is to ensure that there are greater numbers of regulated advisors offering wider access to regulated advice. This will make it imperative that public policymakers do more to promote the affordability and accessibility of regulated financial advice. This is exactly what LifeSearch is attempting to do and we will be happy to share our experience and knowledge with policymakers, especially in light of the partnership with ASDA.

What our experience to date tells us is that one must not under-estimate the FSA's approach to regulating the distribution chain as one of the key factors in explaining the advice sector's slow rate of growth. The FSA's tolerance of those who sell without advice purporting that a product bought in that way is the equal of one bought with advice, even though the suitability rules only apply to the latter, creates competitive disadvantages leading to regulatory arbitrage. This renders advice undervalued by consumers and is helping to drive more and more execution-only sales. This issue should be addressed within the current FSA reviews covering retail distribution and the regulation of general insurance sales, as well inform a central prong in the further development of the Treating Customers Fairly and Financial Promotions regime.