



IFAs may finally be regarded as 'professionals' under the new regime

**RDR SERIES** In the fourth of a five-week series on the RDR, we look at solicitor and IFA links post-RDR as the FSA takes a pragmatic attitude towards independence

# Forging a new life together



IAN  
MUIRHEAD

The original intention of the Retail Distribution Review (RDR) was to distinguish clearly between those financial advisers who share the professional ethic of independence and those whose independence is compromised by their relationship with product providers. In the event, the dividing line seems likely to be blurred, and the only guidance consumers may receive as to the status of advisers is the inclusion of the word 'restricted' in the tied and multi-tied sales pattern.

It may be that the FSA and its political masters took the view that promoting the virtue of independence is less important than maximising the availability of financial advice – or, as some would have it, avoiding further reducing the sector.

A parallel can be drawn with the will-writing market, where the decision was taken not to regulate will writing because this might reduce the availability of the service. One conclusion was that the government would see that it is preferable for a greater number of people to have a will of whatever quality than that a smaller number should have better-quality wills.

However, the fact that the FSA seems to be effectively abandoning its promotion of independence does not mean that it has ceased to be relevant. Independence is a core principle for the established professions, and both the law societies and the accountancy bodies insist their members may only refer their clients to independent advisers for investment advice.

There is further significance in the principle of independence in that, as a result of the Legal Services Act 2007, the established professions are entering a new era in which they will be able to join together in what the Act refers to as alternative business structures. Independent financial advisers are among the potential participants.

## Legal bird

It is solicitors who will experience the greatest change. Pundits have predicted that, as a result of the Act, one-third of the current number of law firms will cease to exist. Some of this decline will be attributable to consolidation, but equally there will be casualties among firms whose business model proves to be uncompetitive.

Historically, solicitors have had two forms of involvement in financial services work. Either they have referred clients to an external adviser, or they have employed advisers to work in-house. Unfortunately, there have been problems with both models.

The external financial advisers were all too often commission-based salespeople who gave solicitors a jaundiced view of financial advisers in general. Moreover, the in-house IFAs more often than not found themselves working among colleagues who made little effort to engage actively with them and who, when serious regulation was introduced by the FSA in 2001, threw in the towel.

The number of law firms now providing an IFA service has reduced from around 750 pre-N2 in 2001 to fewer than 50 today.

So, why should solicitors be starting, as they are, to take renewed interest in financial advice? The answer is they are becoming aware of the need to diversify their business model, to reduce their dependence on transactional activity and to provide a more appealing client service, which will help them build enduring client relationships. The appearance of the professional, fee-based independent financial adviser is, to say the least, timely.

One of the complaints made by solicitors about financial advisers in the past has been that they regarded the referral relationship as a one-way street. It was a source of clients for the IFA that did nothing for the solicitor except expose him or her to the risk of complaint by dissatisfied clients and provide a share of commission, which is a benefit which is now effectively barred by the Solicitors Regulation Authority.

What solicitors are looking for are financial advisers whose skills complement their own and with whom they can form a working relationship. For the adviser this means aligning specialist skills with those of the solicitor, the main areas of common ground being: trusts and estate; older client matters; family relationship breakdown; personal injury trusts and Court of Protection work; corporate;

property; offshore arrangements; and portfolio management. To demonstrate competence and establish rapport, advisers would be well served by obtaining qualifications which resonate with solicitors, in particular the Step (Society of Trust & Estate Practitioners) certificate for IFAs, the Solla (Society of Later Life Advisers) FSSC accreditation; and the Resolution (Solicitors Family Law Association) accreditation for financial neutrals.

An arms-length relationship between solicitor and IFA remains feasible and is indeed likely to be the principal form of association when specialist technical advice is required and the solicitor wants to be seen to be accessing the most suitable source of advice on the market, in the same way as when instructing a barrister. However, referrals are of limited value in enabling the solicitor to develop an integrated legal and financial service and, in the absence of commission, they will provide no financial benefit to the solicitor.

## Close relationship

This has given rise to the sudden popularity of joint ventures – IFA businesses in which solicitors are involved as shareholders but do not provide legal services. Joint ventures offer three main advantages. They create a sense of involvement on the part of the solicitors, who can refer their clients to "our financial services associates".

They enable the solicitors to delegate responsibility for FSA compliance to the IFAs. They also enable the solicitors to draw remuneration in the form of dividends. This last benefit, however, is subject to the important caveat that the joint venture must operate on a fee basis and must account to its clients for any commissions received in the same way as is required by the solicitors' code of conduct.

Joint ventures which operate on a commission basis are regarded by the Solicitors Regulation Authority as devices to avoid the code, and several have been closed down.

Joint ventures can take a number of forms, but the most popular is the model whereby the joint venture is an appointed representative of the IFA firm, which lends its staff and resources and recovers the cost through a management charge. In this scenario the joint venture will usually be formed as a limited liability partnership rather than a limited company, so as to avoid being associated with the IFA firm for tax purposes.

One downside of the joint venture is that its viability will be dependent on the business produced by the law firm participant, and with this in mind some firms have set up multiple joint ventures to service a number of professional firms, with different classes of share for equity participants and referring firms. The group of professional financial centres is an example of this model.

Joint ventures provide a convenient staging post to the multi-disciplinary practices, which the Legal Services Act will permit as from October 2011, and which will be able to provide the basis for different combinations of professionals, providing services focused on client needs rather than similar qualifications. The enterprising law firms Turcan Connell and Dickinson Dees are exponents of this model, although it seems unlikely that many other solicitors will be capable of emulating their commercial acumen.

Multi-disciplinary practices in which solicitors are in the minority are more problematical, having regard to issues such as solicitors' client confidentiality requirements and the disparity between compensation schemes. The solicitors' scheme, for example, offers £1m a claim and the FSCS only £50,000. An alternative which may find favour is the hub-and-spoke model, whereby professional firms – potentially solicitors, accountants and IFAs – would retain their autonomy but form an umbrella service company to provide administration, systems, compliance, marketing and possibly common branding.

Whichever model may be adopted, the conjunction of the Legal Services Act and RDR provides a golden opportunity for IFAs to take their place in the professional community. But the professional regulators have made clear that restricted advisers need not apply.

Ian Muirhead is managing director at Sifa



have your say on this article at  
[www.ftadviser.com/community](http://www.ftadviser.com/community)