

Dynamism in Reforming Financial Product Distribution Channels in the United Kingdom

Kaori ZENIYA

Nomura Research Institute

Dynamism in Reforming Financial Product Distribution Channels in the United Kingdom

Kaori ZENIYA

- I Major Distribution Channels for Financial Products in the United Kingdom
 - 1 Breakdown of Personal Financial Assets in the United Kingdom
 - 2 Major Distribution Channels for Financial Products
- II IFAs Have Built a Firm Position
 - 1 IFAs Handling Products of All Financial Institutions
 - 2 Introduction of the Polarisation Rule
 - 3 Six Types of IFAs
 - 4 Methods Adopted by IFAs to Acquire Customers
 - 5 Services Provided by IFAs
 - 6 Differences between Banks and IFAs
- III Progress in Separating Production and Sales
 - 1 Reducing the Direct Sales Force at Life Insurance Companies
 - 2 Life Insurance Companies Making Use of IFAs
 - 3 Abolition of Polarisation Rules
 - 4 Life Insurance Companies Starting Investments in Large IFAs
 - 5 Acquiring and Retaining IFAs
- IV Suggestions to Japan
 - 1 Distribution Channels Desired by Consumers
 - 2 Establishment of Distribution Channels for Customized Financial Products

In the United Kingdom, life insurance and pensions account for the largest rate among all household financial assets owned. This rate amounts to double that in Japan. Specialists known as independent financial advisors (IFAs) show their significant presence as the distribution channel for such products.

IFAs are financial intermediaries that were given birth by the unique Polarisation Rules in the United Kingdom that require selection between being tied to one company or being independent to handle all products from across the market. The background factor behind the success of IFAs in building their current strong position in the market is not only that one-stop shopping from among all financial products is available through IFAs, but also that IFAs can offer customized financial products to meet customer needs.

Before the 1990s, similar to the situation in Japan, the direct sales force of life insurance companies constituted a major distribution channel in the United Kingdom. However, with the emergence of the Polarisation Rules and the implementation of measures to strengthen compliance, insurance companies promoted the outsourcing of sales activities as part of their marketing strategies. In the course of this process, the insurance companies started to clarify their strategy of focusing on IFAs.

In December 2004, the Polarisation Rules were abolished. Consequently, changes in the distribution channels for financial products are now taking place. At the same time, life insurance companies are further enhancing their structures to support IFAs.

In Japan as well, distribution channels for financial products are now being diversified. In order for financial institutions to survive as leading distribution channels, how they stir up new customer needs will be a key factor in addition to their capability to provide one-stop shopping and their ability to sufficiently meet existing consumer needs.

In Japan’s retail financing market, rapid progress is about to be made in the diversification of product distribution channels with the over-the-counter sale of unit trusts/OEICs at banks as the start, followed by permission of the OTC sale of some life insurance products at banks and securities brokerage by financial institutions other than securities firms. The “Program for Further Financial Reform—Japan’s Challenge: Moving toward a Financial Services Nation,” which was announced by the Financial Services Agency in December 2004, outlines the priority issues of financial administration for the next two years. One of the goals included in this program is the “enhancement of the provision and distribution framework for financial products and services.”

Turning our eyes to the situation in the United Kingdom, we see a long history of the diversification of distribution channels. The tendency to separate production and sales has already been seen for over ten years. In such a long history of diversification, what distribution channels have been accepted by consumers? This paper attempts to identify the issues that should be strengthened in establishing distribution channels in Japan by summarizing the features of the retail market in the United Kingdom.

I Major Distribution Channels for Financial Products in the United Kingdom

1 Breakdown of Personal Financial Assets in the United Kingdom

As indicated in Figure 1, the rate of life insurance and pensions is high at 54.1 percent among household financial assets in the UK. This rate is almost twice that of Japan, and also is higher in comparison with other coun-

tries. This high rate can be regarded as one of the characteristics of the UK.

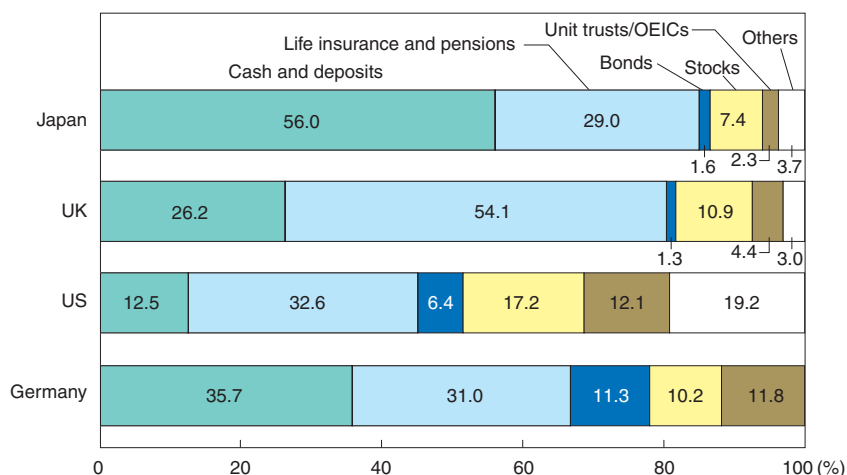
In the United Kingdom, where the concept of life insurance was first born, the ownership rate of life insurance and pensions has been high for a long time. What further facilitated the increase of this rate was the pension reform implemented in 1988 during the Thatcher administration. For the purpose of reducing the government burden, it was recommended that the portion proportional to remuneration that corresponds to the second tier of the two-tier structure of the government pension scheme be changed to a personal pension plan. The increase in the number of persons subscribing to a personal pension plan in response to such recommendation has contributed to the increase in the said ownership rate. The fact that the stock market and the real estate market have been in good condition throughout the 1990s can be cited as another reason for the increase in the ownership of life insurance products.

2 Major Distribution Channels for Financial Products

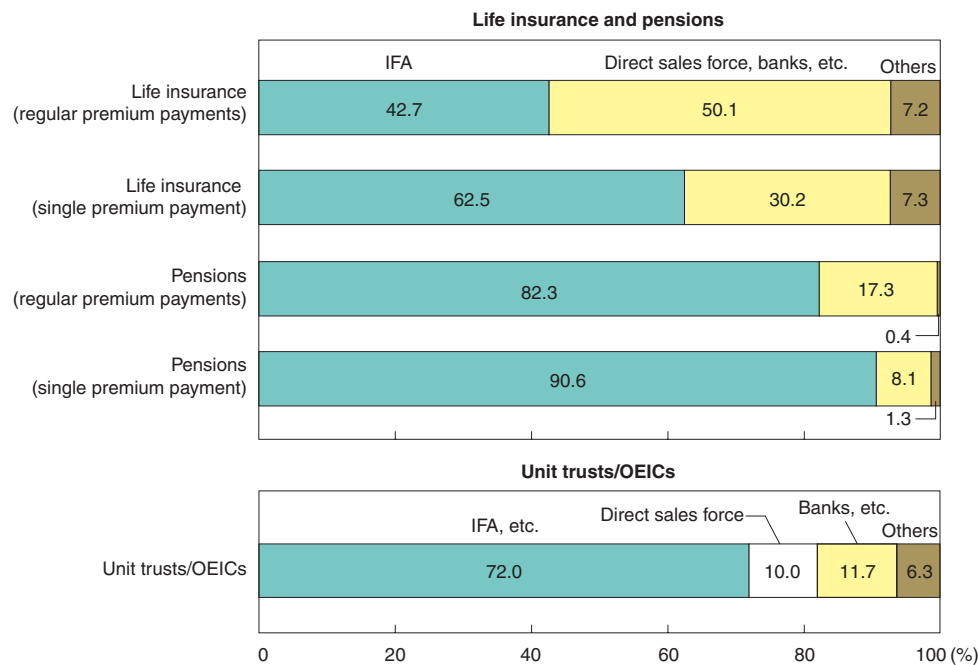
In purchasing these life insurance and pension products, British citizens select a channel suitable for themselves from among a wide variety of distribution channels. In the same way as in Japan, people can purchase products directly from sales representatives of life insurance companies and can also buy them at banks. In addition, they can purchase them at supermarkets where perishable foods and daily necessities are sold.

While such a wide variety of distribution channels are available to purchase life insurance and pension products, independent financial advisers (IFAs), which are described in subsequent chapters (Figure 2), account for the largest share among these channels in terms of the sales amount. Furthermore, IFAs also constitute a major channel in the sales of unit trusts/OEICs.

Figure 1. Breakdown of Personal Financial Assets in Major Countries (As of the end of 2003)



Sources: Japan: the Bank of Japan; UK: UK Office for National Statistics; US: Board of Governors of the Federal Reserve System; Germany: Deutsche Bundesbank.

Figure 2. Financial Product Distribution Channels in the United Kingdom

Note: Revenues from premiums in 2004 are totaled by distribution channel.

Source: Compiled based on materials of the Association of British Insurers and the Association of Investment Trust Companies.

II IFAs Have Built a Firm Position

1 IFAs Handling Products of All Financial Institutions

Independent financial advisers are financial intermediaries who chiefly handle collective investment schemes consisting of life insurance, pensions, unit trusts/OEICs, etc. Passing a qualification test is necessary to become an IFA. There are many cases in which persons who accumulated experience at life insurance companies, etc., acquire qualification and become independent advisors.

As the name suggests, an IFA is independent of any of the institutions providing financial products (e.g., life insurance companies) and handles products of all financial institutions, which can be regarded as an attribute of an IFA. IFAs are prohibited from handling the products of one or multiple specified companies. This rule is known as the Polarisation Rule.

2 Introduction of the Polarisation Rule

In the United Kingdom, the Financial Services Act was established in 1986 and came into effect in 1988 for the purpose of protecting consumers of financial products. In a broader sense, this is considered as one of the Big Bangs. Pursuant to this Act, multiple independent regulatory organizations were established. This Act required financial institutions to belong to one of these regulatory organizations and to conform to its regulations.

Before the enforcement of the Financial Services Act, life insurance products were sold by sales representatives of life insurance companies and insurance brokers. While registration was required to represent oneself as an insurance broker, life insurance products could be sold without being subject to regulation if one did not use the name of an insurance broker. As such, there was a loophole that may have given rise to mis-selling. After the enforcement of the Financial Services Act, controls on salespersons were strengthened, such as that a criminal penalty is now imposed if a person engages in sales activities without registering with the self-regulating organization.

The Act requires persons who sell financial products without working for either a life insurance company or a bank, such as IFAs, to register with the independent regulatory organization known as FIMBRA (Financial Intermediaries, Managers and Brokers Regulatory Association).¹ Under FIMBRA's rules, IFAs must be independent of any insurance companies, and must handle the products of all life insurance companies.

In contrast, life insurance companies and exclusive agents of life insurance companies must belong to the independent regulatory organization known as LAUTRO (Life Assurance and Unit Trust Regulatory Organization).¹ Under LAUTRO's rules, salespersons can only handle the products of their own companies or contracted companies.

As such, the rules that require IFAs to cover the products of all life insurance companies, but prohibit exclusive agents of life insurance companies from selling products of other companies, are called the Polarisation Rules.

The fact that mis-selling of financial products prevailed can be cited as a background factor behind the introduction of these rules. The Polarisation Rules are based on the concept that in order to protect consumers from mis-selling, it is necessary to distinguish between salespersons who are independent and provide advice on products from the customer standpoint and salespersons who recommend products as agents of financial institutions.

It can be said that the introduction of the Polarisation Rules has essentially given rise to IFAs.

3 Six Types of IFAs

About 60,000 qualified persons can provide advice on financial products in the United Kingdom. Of these, about 30,000 persons either are affiliated with financial institutions or have a contract with a single specified financial institution. Among the remaining 30,000 persons, about 4,000 are qualified financial advisers who have professional jobs as their principal business, such as solicitors and accountants. Accordingly, after deducting these 34,000 from the total of 60,000 persons, 26,000 persons can be regarded as IFAs.

If IFAs are classified by organization, they can be divided into six types as indicated in Figure 3, i.e., “IFA networks,” “national IFAs,” “big IFAs,” “regional IFAs,” “network members” and “small IFAs.” Because network members and small IFAs who are either individuals or organizations close to individuals account for more than 90 percent of all IFAs, many IFAs conduct sales activities by maintaining a close relationship with their community.

IFA networks function as organizations that provide services such as responding to regulatory changes and providing compliance advice (law observance) to small-sized IFAs that are close to individual sales activities; there are approximately 15 such networks. Their major

duties include negotiations with life insurance companies to obtain more advantageous commissions, which constitute one of the major reasons IFAs with limited negotiating ability join an IFA network.

4 Methods Adopted by IFAs to Acquire Customers

IFAs rarely use advertising or publicity. Their offices neither face a main street nor have an eye-catching signboard. A typical IFA office is located at the corner of a residential area, and a small signboard is put up at the entrance. What is written on the signboard is barely understandable without careful reading, which hardly qualifies it as a signboard. In other words, their offices are not located where there is a lot of pedestrian traffic, but are places to visit after an appointment is made. This situation suggests that IFAs do not acquire customers by advertising to the public.

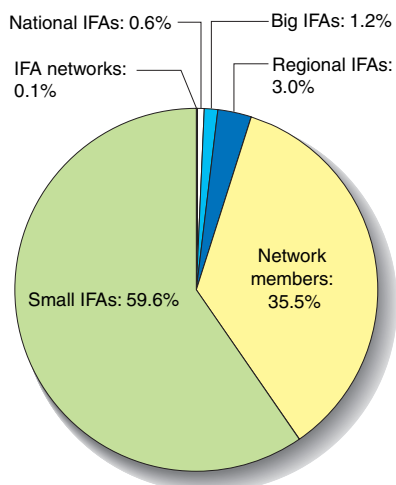
In actuality, IFAs acquire customers by introductions from existing customers (word of mouth) and introductions from solicitors and accountants in the area. Accordingly, customers are inevitably limited to the wealthy segment.

5 Services Provided by IFAs

A wide selection of products is frequently cited as one of the reasons IFAs have penetrated into the wealthy segment. However, this is not the primary reason.

If each financial product is seen as a component, IFAs assemble such components in accordance with customer needs and provide value-added products by creating customized financial products. Because a major method for IFAs to acquire customers is introduction from solicitors and accountants, how to incorporate tax reduction measures in the customized product is where they can best show their skills. Good workmanship can

Figure 3. Types of IFAs by Scale



- (1) IFA network: An organization of 10 or more independent IFA companies. The IFA network itself obtains approval from the FSA and does the following with respect to the activities of IFAs within the network: submitting reports to the FSA, checking compliance, providing education and guidance, providing systems, etc.
- (2) National IFAs: Any firm with a turnover of 5 million pounds or more, or 10 or more outlets
- (3) Big IFAs: All firms with one outlet and a turnover of 1 million pounds or more
- (4) Regional IFAs: Firms with two or more outlets
- (5) Network members: IFAs belonging to one of the IFA networks indicated in (1)
- (6) Small IFAs: Remaining single outlets

Note: FSA = Financial Services Authority.
 Source: Tillinghast-Towers Perrin, *Insurance Pocket Book 2005*, NTC Publications.

lead not only to retaining existing customers but also to acquiring new customers through introduction by existing customers.

Figure 4 shows an example of a customized product that incorporates inheritance measures for which IFAs are skillful. Specifically, funds are borrowed from a life insurance company by using a house as collateral in the form of equity release.² In so doing, a trust account is established in which the funds are managed. These funds are operated by an investment bond (terminable investment securities), which is one of the investment products of a life insurance company. In the United Kingdom, taxable assets for an inheritance tax consist of assets to be transferred at the time of the death of a legator and assets donated or transferred seven years before the death of a legator. The mechanism incorporated in this product to reduce taxes is to establish a trust account wherein the beneficiary receives assets after the elapse of at least seven years.

As explained above, consulting sales activities for financial products and services such as those conducted by IFAs become a successful business only when they organize a highly value-added product offering a rather high commission.

6 Differences between Banks and IFAs

In the United Kingdom, banks also handle various financial products. Life insurance and pensions are also positioned as major products. While there are exceptions, a bank primarily provides products by concluding an exclusive contract with a single life insurance company (called a tied agent).

Unlike IFAs, bank counters are seen as places where commodity products are sold. In other words, customers visiting a bank have already decided on the product they intend to purchase and do not expect any advice at the bank counter. As a difference between tied agents such as banks and IFAs, attention tends to be directed towards the number of life insurance companies and unit trust/OEIC operation companies whose products are handled. However, a major difference appears to be that one is merely selling components and the other is providing customized products by combining components.

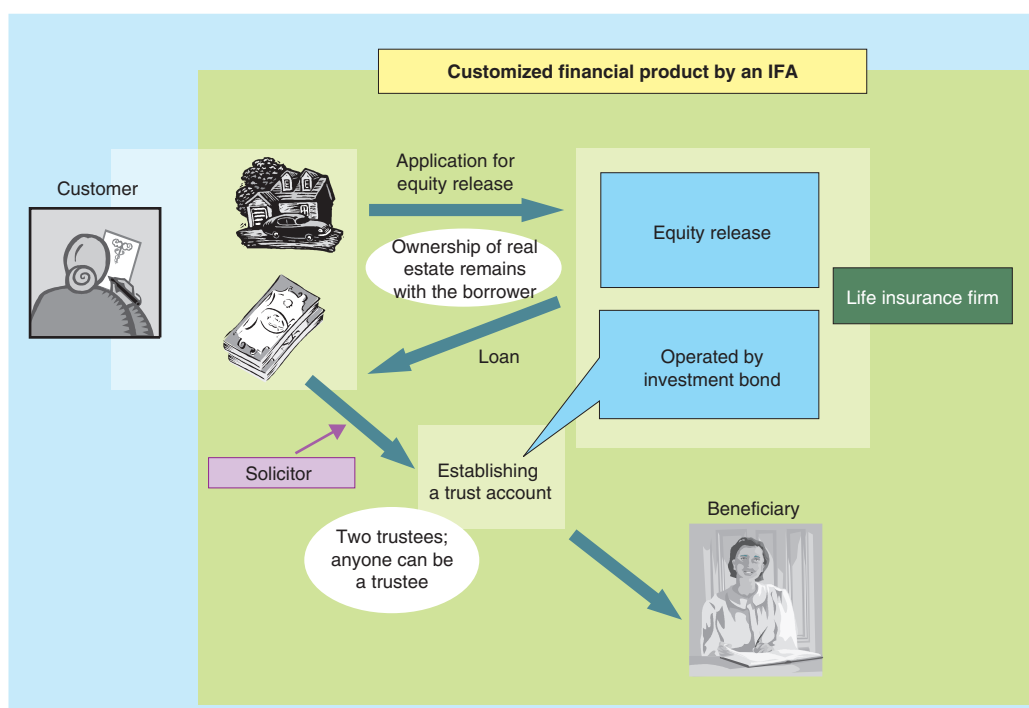
For example, HBOS, which is one of the leading banking groups, has two affiliated insurance companies. Halifax Life, which is one of these insurance companies, offers products to be handled at bank counters. The other life insurance company, Clerical Medical, develops products to be sold through IFAs. According to an explanation by HBOS, the former offers products made of a simple mechanism and the latter offers products enabling complicated combinations. This suggests that life insurance companies also entrust IFAs to handle life insurance products and pensions having complicated features.

III Progress in Separating Production and Sales

1 Reducing the Direct Sales Force at Life Insurance Companies

As explained in the previous chapters, it is possible to purchase life insurance and pension products through a

Figure 4. A Customized Financial Product by an IFA



variety of channels in the United Kingdom. Salespersons of life insurance companies represented a major distribution channel until the 1980s in the same way as the current situation in Japan (Figure 5). However, in early 1990, the ratio of sales through a company's own salespersons began to gradually decline. This trend can reasonably be interpreted as a result of changes in the sales strategies of the life insurance companies.

Since the enforcement of the Financial Services Act, stronger measures have been taken to ensure compliance. In order to avoid the cost increases accompanied by strengthened compliance measures, life insurance companies started to adopt strategies to reduce the sizes of their own sales forces. According to an estimate by a major life insurance company, the cost of using its own sales force is higher by some 30 percent than the cost of using IFAs. The increased burden in administrative, auditing and compliance functions weakened the advantage of having their own sales forces, leading to reductions in the sizes of direct sales forces.

Another background factor that necessitated cost cutting by reducing the sizes of sales forces is that personal pension plans were mis-sold during the latter half of the 1980s, and a need arose to cover the costs of litigation for this purpose. Personal pension mis-selling is related to pension reform that was implemented due to the high proportion of life insurance and pensions in the United Kingdom, as explained previously. When a shift to a personal pension plan was recommended as part of pension

reform, it was even recommended to persons who were nearing retirement and for whom it was essentially more advantageous to continue their existing pensions proportional to remuneration. This issue has developed into a societal issue.

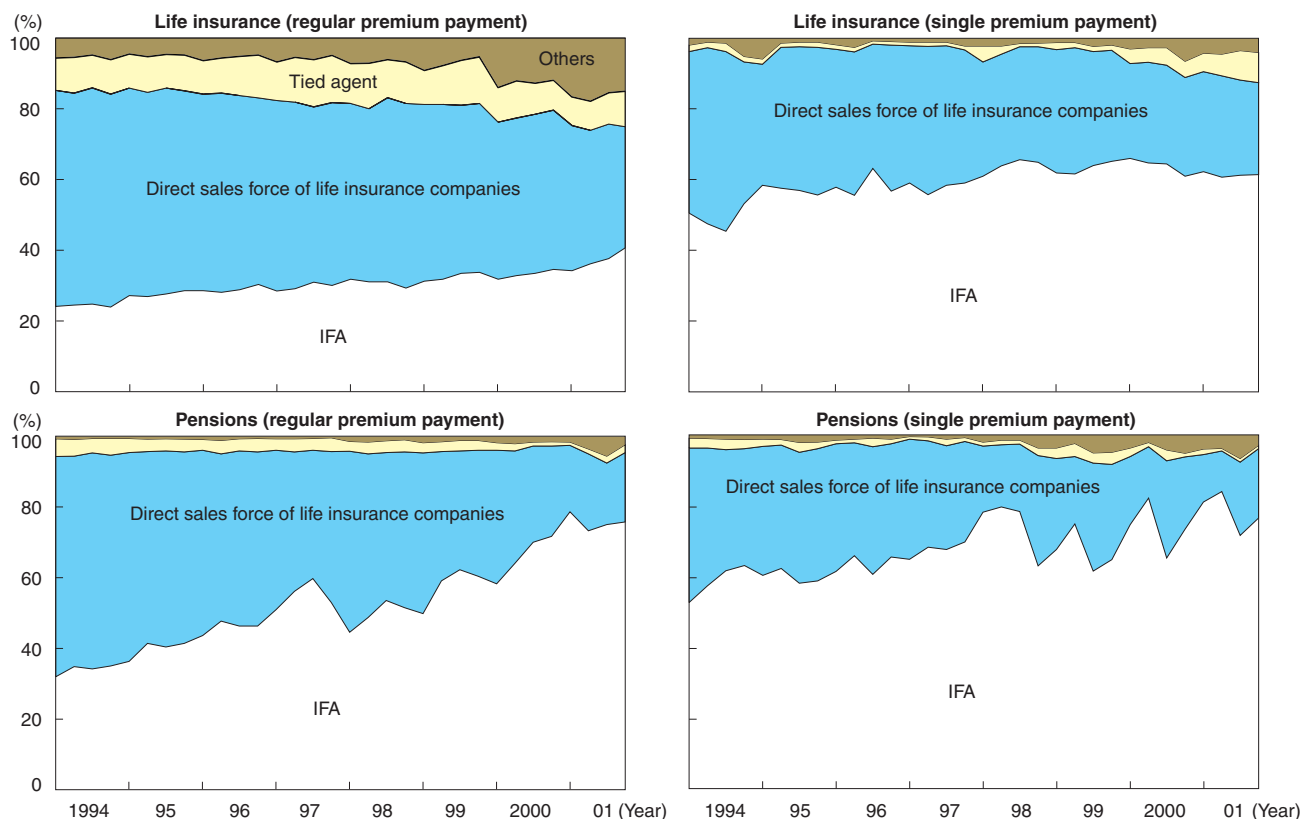
According to interview surveys by IFAs, the personal pensions were mis-sold chiefly by the direct sales forces of life insurance companies. Table 1 outlines details related to redress accepted in relation to such mis-sales of personal pensions that were announced by the Financial Services Authority (FSA). An overwhelming number of cases involved life insurance companies and bancassurance, and these data support that mis-selling was principally conducted by their own direct sales forces.

The pension review was implemented in two phases. In Phase 1, priority was given to senior consumers at or near retirement. Approximately 421,000 persons received redress during Phase 1; the total redress amount reached 4 billion pounds (about 800 billion yen). In Phase 2, as well, the total redress amounted to the same level. As such, personal pension mis-selling resulted in an extremely heavy burden.

2 Life Insurance Companies Making Use of IFAs

As described above, life insurance companies in the United Kingdom promoted the separation of production and sales as part of their sales strategies. In the course of

Figure 5. Changes in Distribution Channels for Life Insurance and Pensions



Source: The Association of British Insurers.

Table 1. Details of Phase 2 Pension Review

	Total	Product providers and bancassurers	IFA networks, big IFAs	Small IFAs
Request for review (unit: persons)	1,248,631	1,085,856	103,185	59,590
Cases reviewed (unit: persons)	833,124	743,159	53,466	36,499
Assessment completed (offers made plus cases where no redress was due) (unit: persons)	699,455	629,594	47,690	22,171
Total amount of redress accepted (unit: million pounds)	4,431	3,934	406	90

Notes: (1) The personal pension mis-selling review was aimed at people who were incorrectly sold personal pensions between April 29, 1988, and June 30, 1994. (2) This review was divided into Phase 1 and Phase 2. Phase 1 targeted persons for whom urgent measures were necessary, such as those who had already retired or who were nearing their retirement age. Phase 2 extended the review to younger individuals. (3) The number of persons for whom assessment was completed is the total number through December 2001. Source: FSA's press release (January 28, 2002).

this move, IFAs started to carry great weight as a distribution channel.

Life insurance companies have established a framework of working closely with IFAs by assigning personnel who are responsible for liaison with IFAs in each area. Norwich Union, the largest life insurance company, has 16 representative offices throughout the country, with each representative office having a staff of 25 including those who are in charge of clerical work. These staff members do not engage in sales activities, but specialize in liaison with IFAs. There are only a limited number of offices (4 – 5 offices) for the direct sales force throughout the country. This also suggests that life insurance companies consider IFAs as important distribution channels.

3 Abolition of Polarisation Rules

While it is not an exaggeration to say that the Polarisation Rules gave rise to IFAs, this regime has twice been criticized by the director general of Fair Trading in 1998 and 1999 as impeding fair competition. Accordingly, this regime was to be reviewed.

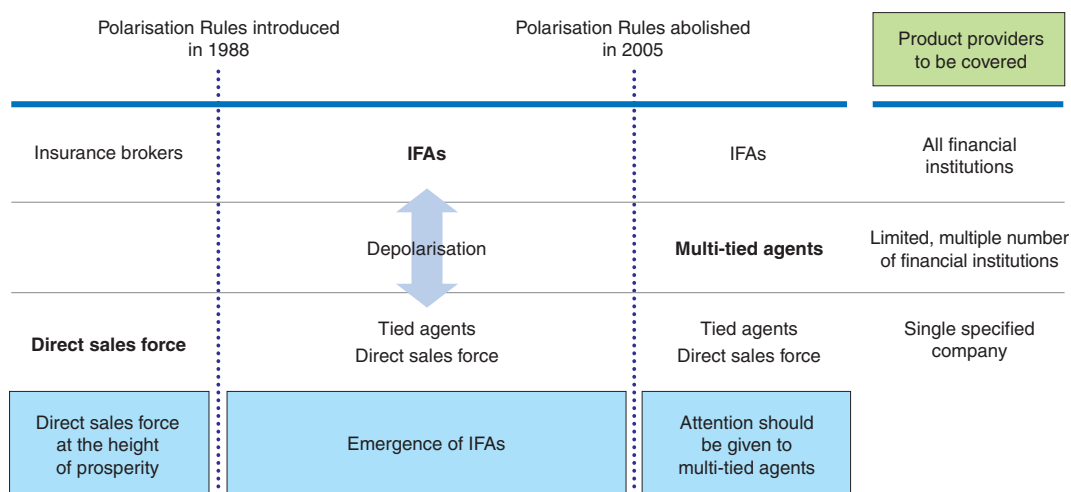
At present, FSA is the sole regulatory organization supervising all financial institutions in the United Kingdom, and has taken over the functions performed by LAUTRO and FIMBRA in the past. FSA announced the review of the Polarisation Rules in January 2001, and abolished this regime as of December 1, 2004, after having discussions with those concerned with this industry over several years.

The abolition of the Polarisation Rules meant that products of specified multiple financial institutions could be handled. Specifically, an intermediary format of multi-tied agents became available in addition to the bipolarity constituted by tied agents and IFAs (Figure 6).

Because this decision is expected to facilitate the shift from both tied agents and IFAs to multi-tied agents, life insurance companies that are financial institutions offering products consider the measures for multi-tied agents as being most urgent.

This is because the number of life insurance companies that are selected by multi-tied agents is said to be six companies at the maximum; whether a company is included in this limited coverage is an extremely far-reaching

Figure 6. Changes in Major Distribution Channels from the Introduction to the Abolition of Polarisation Rules



issue. Many observers forecast that the abolition of the Polarisation Rules will reduce the number of insurance companies. As such, the need has arisen to appeal a company to tied agents and IFAs who are expected to shift to multi-tied agents.

4 Life Insurance Companies Starting Investments in Large IFAs

As explained above, it has become a major strategic issue for life insurance companies to secure distribution channels. As a means of resolving this issue, life insurance companies have started to invest in large IFAs and IFA networks. Because life insurance companies expect that many large IFAs in particular will become multi-tied agents, they are embarking on strategies focused on securing future distribution channels by investing in IFAs. The largest company, Norwich Union, has invested in all three major IFA networks (Sesame, Bankhall, and Tenet).

Under the current rules, if a life insurance company invests 10 percent or more in an IFA, the invested IFA is prohibited from selling the products of the investing life insurance company.³ However, some life insurance companies are striving to secure distribution channels in preparation for the future even by investing 10 percent or more. Aegon UK, which is one such life insurance company, acquired a regional IFA company, Wentworth Rose, in June 2002. Starting with this acquisition, Aegon purchased five regional IFA businesses. While review of the Polarisation Rules was announced in January 2001, such moves represent prior investment under circumstances where the direction of the review has not yet been clarified.

Aegon UK integrated the five IFA businesses it acquired to form Origen. Under the brand name of Origen, sales activities were started in May 2004. In the initial year after integration, the number of advisors was 200, and annual sales were 36 million pounds (about 7.2 billion yen). Goals for 2008 were set at 400 advisors and 90 million pounds (about 18 billion yen).

Aegon UK is the local company of Aegon in the United Kingdom, which is one of the three leading life insurance companies in the Netherlands. Aegon has adopted the strategy of regarding Production, Asset management and Distribution as its three major revenue sources. The "Production" function, which corresponds to the development of life insurance products, is performed by Scottish Equitable, which was acquired. Because the brand name of Scottish Equitable is more widely recognized in the United Kingdom, business activities could continue without changing the name of the company after its acquisition.

The "Asset management" function is performed by Aegon Asset Management, and the "Distribution" function is performed by Origen. Because it conducts business activities as an IFA firm, under the current regulations,

Origen cannot sell the products of Scottish Equitable. Nevertheless, Aegon UK expects to secure revenue by relying on the sales capabilities of Origen and considers Origen as an important distribution channel in the future for the products of Scottish Equitable.

In addition, Aegon UK also invested 9.9 percent in Tenet, a major IFA network.

However, it is worthy of special mention that while strengthened efforts are being made to secure distribution channels, a declining trend is still seen with respect to the direct sales force of life insurance companies.

5 Acquiring and Retaining IFAs

Measures to acquire and retain IFAs are also seen in activities other than investment. At present, in the United Kingdom, the provision of wrap service is being promoted by following the examples of the United States and Australia that introduced wrap service. The first participant in the wrap market in the United Kingdom is Transact, whose parent company is in Australia. Subsequent participants include a range of life insurance companies. Wrap service is expected to be offered not only by multi-tied agents but also by all types of IFAs.

It should be noted that the wrap service provided in the United Kingdom is different from that offered in the United States. Under wrap service in the United States, a securities firm (or an investment management company having a contract with a securities firm) concludes an investment discretionary contract with an investor concerning trades using an account established at the securities firm, and provides fund management services. Because brokerage commissions and account management fees are included together with investment advisory fees, this service is called wrap service.

In contrast, wrap service in the United Kingdom is an account aggregation service where all account information of multiple financial institutions is collectively managed in combination with the mechanism of trading financial products.

In addition, there are two more major features. In the United Kingdom, preferential tax treatment is available for several types of financial product investment instruments. The first feature is that wrap service is also designed to provide these instruments in addition to the integrated offering of individual deposits, stocks, unit trusts/OEICs, life insurance, pensions and real estate.

The second feature is that all companies providing wrap service give priority to the use of such services by IFAs. Rather than positioning wrap service as a new service, they are designing this service as a support tool for IFA activities. From the standpoint of IFA users, it has already become possible to purchase financial products on a one-stop basis and to receive a comprehensive report indicating the value of financial assets after purchases. However, this service is now achieved by means

of the manual work of IFAs. The provision of infrastructure for this manual work portion will directly lead to the improvement of the efficiency of IFAs and eventually to the reduction of the clerical expenses of life insurance companies themselves.

Norwich Union plans to start a wrap service developed by Lifetime Group, an IT (information technology) vendor, and has started trial operations by establishing a partnership with Millfield Group, a leading national IFA firm, prior to the start of full-scale operations. As Norwich Union has already invested in Millfield,⁴ it is trying to doubly strengthen its relationship with Millfield through the introduction of wrap service.

In March 2005, Friends Provident, a major life insurance company, announced the start of DPP (dynamic portfolio planner) service. Although this is not a wrap service, it is a system developed for IFAs. Based on customer information entered into the system, this service automatically suggests an asset selection plan suitable for an individual investor. In addition, this system is equipped with unit trust/OEIC research information, unit trust/OEIC selection functions and compliance check functions. Friends Provident positions DPP as a means of providing additional support for IFA activities.

IV Suggestions to Japan

1 Distribution Channels Desired by Consumers

This paper has so far outlined the distribution channels for life insurance and pensions in the United Kingdom. The framework has also been established in the United Kingdom to purchase other financial products through a variety of distribution channels.

Answers to the question of why IFAs have been accepted under the circumstances where a wide array of distribution channels is available involve four features. First, IFAs are independent from financial institutions. However, it is not the case that IFAs are recognized as independent because they merely handle the products of all financial institutions. The standard for being independent is whether they recommend products from their customers' perspectives. On the part of IFAs as well, unless they secure the trust of their customers, they may even lose their existing customers, far from acquiring new customers who are introduced by existing customers. It can be said that IFAs who are capable of retaining their existing customers are surviving in the market.

The second feature relates to whether a single IFA can fulfill all customer needs. Banks are the most familiar financial institutions to the general public in the United Kingdom as well as in most parts of the world. Banks are well known among most people and, although the

number of financial institutions whose products are handled is limited to one, almost the same selection of financial products is available as that of IFAs. Considering the fact that banks also serve as intermediaries for stock trades, the number of financial products handled by banks is quite a bit greater than those handled by IFAs.

However, the failure of banks to improve their share of life insurance and pensions is attributable to the situation in which different sections are responsible for each product type and a customer must consult with different personnel for each product, whereas a single IFA can cover all the products needed. While one-stop service is available from the viewpoint of an entire bank, the customer ends up purchasing mere components because different departments are involved.

The third point involves a concept of negativity. The fact that banks in the United Kingdom are not so strongly trusted as those in Japan appears to be partly attributable to the establishment of a mindset of relying on IFAs whenever advice is needed.

Last, it is significant that IFAs are able to obtain backup from life insurance companies for the improvement of IFA services, with a resulting increase in sales performance by IFAs.

2 Establishment of Distribution Channels for Customized Financial Products

This paper has also indicated that the existence of IFAs as one of the distribution channels for financial products is significant in the United Kingdom. In light of the fact that the unique Polarisation Rules served as a trigger in giving rise to IFAs in the United Kingdom, an environment is by no means present in Japan in which a scheme similar to IFAs can function immediately. While the fostering of financial advisors has already started in Japan, financial institutions in their capacity as distribution channels are taking the lead in such endeavors. This suggests that the Japanese equivalent to IFAs is most likely to be developed in the form of being a part of existing financial institutions, such as securities firms, city banks, regional banks, credit associations and credit cooperatives.

With progress in the diversification of distribution channels, the trend toward one-stop shopping for financial products is being accelerated. However, what is envisioned at the current stage is simply the ability to purchase individual financial product components at a single location. The efforts of financial institutions in this regard have not yet reached the level of providing customized products that meet individual needs by freely combining components. In addition, in order to develop customized products, it is necessary to obtain a customer's personal information, such as the structure of the family, financial assets owned, investment objectives and future plans. Even though the reliability of financial institutions is already high in Japan, it would be necessary to make additional efforts to build a foundation to enable

consulting sales activities by gaining further customer confidence.

In the future, financial institutions that can actively draw on the needs for customized products in addition to the ability to meet the requirements indicated above will be likely to grow as the leading distribution channels in Japan.

General note

This paper is based on information available as of May 2005.

Specific notes

- (1) FIMBRA and LAUTRO were integrated into a single regulatory organization, the Financial Services Authority (FSA).
- (2) In the United Kingdom, a reverse mortgage (a mechanism in which a senior borrows money on a regular basis by using a house as collateral, and this house is sold when the senior dies to collectively repay the loans) is called equity release.
- (3) This rule doesn't apply in all cases. An IFA can sell the products of an investing company if it can be demonstrated that their products are superior to all similar products of all other financial institutions.
- (4) In addition, Aegon, Friends Provident, Scottish Widows and Skandia have invested in Millfield.

References

1. Financial Services Agency, "Program for Further Financial Reform—Japan's Challenge: Moving toward a Financial Services Nation," December 2004.
2. Hirofumi Ushikoshi, *Kin'yu sabisu ho: seiho, nenkin, toshin hanbai no besuto adobaisu o mezashite* (Financial Services Law: Providing the Best Advice for the Sales of Life Insurance, Pensions and Investment Trusts), Kinzai Institute for Financial Affairs, 1999.
3. Japanese Institute of Certified Public Accountants, "Sozoku, zoyo ni kakaru zeisei ni tsuite: sozokuzei to zoyozei no ittaika no hokosei" (Taxation concerning Inheritances and Gifts: Direction toward the Integration of Inheritance Tax and Gift Tax) (Taxation and Legislation Research Committee Research Report, No. 13), December 2004.
4. Datamonitor, "UK Independent Financial Advisors 2002," May 2002.
5. FSA, "CP80: Reforming Polarisation—First Steps," January 2001.
6. FSA, "PS04/27: Reforming Polarisation: Implementation—Feedback on CP04/3 (A menu for being open with consumers) and made text," November 2004.

Kaori ZENIYA is a chief researcher at Nomura Research Institute Europe Limited. Her specialties include retail banking market research.

As a leading think tank and system integrator in Japan, Nomura Research Institute is opening new perspectives for the social paradigm by creating intellectual property for the benefit of all industries. NRI's services cover both public and private sectors around the world through knowledge creation and integration in the three creative spheres: "Research and Consulting," "Knowledge Solutions" and "Systems Solutions."

The world economy is facing thorough structural changes led by the dramatic growth of IT industries and the rapid expansion of worldwide Internet usage—the challenges of which require new concepts and improvement of current systems. NRI devotes all its efforts to equipping its clients with business strategies for success by providing the best in knowledge resources and solutions.

NRI Papers present selected works of NRI's 3,000 professionals through its worldwide research network. The mission of *NRI Papers* is to contribute new ideas and insights into business management and future policy planning, which are indispensable for overcoming obstacles to the structural changes in our society.

All copyrights to *NRI Papers* are reserved by NRI. No part of this publication may be reproduced in any form without the prior written consent of NRI.

Inquiries to: Corporate Communications Department
Nomura Research Institute, Ltd.
E-mail: nri-papers@nri.co.jp
FAX: +81-3-5533-3230