Ownership bias a concern in finance industry

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COMMENT

The Government is in the process of limiting the way commissions can be paid in the financial planning industry. These reforms are intended to deal with the conflict of interest that happen when a financial planner is paid on the basis of what is bought by clients.

While these reforms are important they will not deal with an equally important issue, which is known as ownership bias.

Ownership bias is caused by the way the financial planning industry is arranged. A car dealership is part of an integrated distribution pipeline that extends from the manufacturer of the car to the salesman that you are talking to. By integrated I mean everyone involved works together with the sole objective of selling as many cars and making as much money as possible.

A big part of the financial planning industry operates in the same way. The process starts with the product manufacturer. Just like a car maker, big financial institutions manufacture financial products that then have to be sold to customers.

To sell their products, these institutions use their distribution pipeline. This pipeline consists of financial planning firms that are owned or controlled by the manufacturer. Importantly, unlike a car dealer, financial planning firms don't advertise the fact they are associated with a particular manufacturer and may often have a different name so that the link between them and the manufacturer is not obvious.

This is done to try to stop you working out that rather than receiving unbiased financial advice you are really being sold financial products made by one company in the same way that a car salesman will try and sell you a particular brand of car.

Your financial planner is at the end of the manufacturer's product distribution pipeline. Just like a car salesman they will get commissions depending on the number of financial products that are sold to you. This causes its own set of problems.

However, just as importantly, they are part of a system that is designed, like the car industry, to sell products made by one manufacturer to you. A car salesman never says that some other brand of car would be better for you, their job is to sell only a particular brand of car. Financial planners who work for financial planning firms that are owned or controlled by a product manufacturer are doing exactly the same thing, selling one brand of financial product to you.

Under the current regulatory system, this obvious problem is meant to be solved by disclosure. When you visit a financial planner you will be given documents called a financial services guide and a statement of advice.

Where your financial planner is linked to a product manufacturer that link has to be disclosed in these documents. When you get them you should look for these types of disclosures and think about what they mean for the quality of the advice being provided to you.

For every financial product there will often be multiple and sometimes hundreds of alternative products.

If you are being sold products that were all made by the same company, you should assume that your financial planner is, in some way, linked to that company.

The Government does not appear to be interested in dealing with ownership bias. Things will change when customers refuse to deal with financial planners who are owned or controlled by product manufacturers.

Information about whether your financial planner works for a product manufacturer is easy to get. Once you work that out, you need to think carefully about whether that arrangement is really in your best interests.

David Huggins is a lawyer who specialises in resolving disputes about poor financial advice