

## Article

### Half empty or half full?

26th February 2009

The SIPP market is experiencing growth, development, challenges and change all at the same time. Volatile market conditions, the results of a thematic review and discussions about improving comparability when transferring to a SIPP are the hot topics.

Is the SIPP growth bubble about burst? This will often depend on whether you sit in the camp of the optimists or pessimists. It was Winston Churchill who said, “the pessimist sees difficulty in every opportunity, the optimist sees the opportunity in every difficulty.”

#### September 2008

On 29th September 2008 the FSA published a press release making it clear that they expect firms to ensure that suitable advice is provided on any transfer to a SIPP. This provided details of the Handbook Notice (81) that confirmed changes to the FSA Conduct of Business Sourcebook to implement the SIPPs (Contracting Out) Instrument 2008.

The release outlined clearly that the FSA expects firms to ensure any advice to transfer is suitable and based on an assessment of the customer needs to help consumers make decisions that are right for them. This is consistent with other areas of the pension market, makes a great deal of sense and should be supported.

It then goes on to say that this would include determining whether there is a genuine need for the investment flexibility and control associated with a SIPP. You must provide a clear explanation of the costs involved and how the recommendation meets a customer’s needs and attitude to risk. This highlights an area where I believe a greater understanding of the variety of SIPP structures available is needed. I will return to this point later.

#### December 2008

The FSA report on the quality of advice on pension switching was issued on Friday 5th December 2008. It summarised the findings of recent thematic work looking at advised transfers to Personal Pensions including SIPPs.

Part one of the review assessed the quality of advice given to customers since A-Day to switch their existing pensions into a personal pension plan (PP) or self invested personal pension (SIPP), the firms’ systems and controls relating to this advice.

Part two assessed whether the actions of pension providers affected the quality of this advice.

#### Findings

The FSA visited 30 adviser firms, assessing 500 files and found that the advice was unsuitable in 16% of cases. A number of reasons were provided as examples.

- The switch involved extra product costs without good reason (79% of unsuitable cases). Reasons for switching included:
  - investment flexibility, but this was not likely to be used;
  - flexibility of an income drawdown option, with no evidence that this was needed;
- The fund(s) recommended were not suitable for the customer’s attitude to risk and personal circumstances (40% of unsuitable cases);
- The adviser failed to explain the need for, or put in place, ongoing reviews when necessary (26% of unsuitable cases); and
- The switch involved loss of benefits from the ceding scheme without good reason (14% of unsuitable cases).

The FSA will be putting in place a range of measures depending on the extent of each firm’s failings and will require them

to address any unsuitable sales.

The FSA did not have serious concerns about the way the pension providers visited had been marketing their products to advisers. However, they were concerned that some seemed unlikely to be complying with the requirement to use lower projection rates where the standard rates would overstate the investment potential. The example provided covered cases where 5%, 7% and 9% projections were included on cash deposits. The FSA will be following this point up with the firms concerned.

Initial press coverage suggested that the issues and problems identified in this thematic review related to the SIPP market. The report simply does not provide sufficient information to identify whether the cases involved were transfers to SIPP or Personal Pensions. Recent correspondence with the FSA has confirmed that the thematic review was structured to assess the common risk of unsuitable advice for customers switching into both product types. The sample selected was broadly representative of the market for advised switches into Personal Pensions and SIPPs. I think it is important to draw a line under any confusion on this point, the FSA have made it clear that the methodology adopted did not attempt to make a comparative assessment between SIPPs and PPs.

### **SIPP versus Personal Pensions**

For many advisers and clients, SIPPs are viewed as Personal Pensions with a wider investment choice. The market historically aligned itself around three distinct variants.

The first could be described as the conventional SIPP, dealing in all areas from share portfolios and collectives to commercial property.

The second, typically a lower cost option, which offers access to a wide range of investments but does not venture into the more labour intensive assets like commercial property. This helps to keep the costs down, often below those on offer from insured personal pension products with external fund links.

The third variant is the low cost execution only model, which appeals to those who rarely take advice and want to adopt a DIY approach. Clients using this model tend to be outside of the advice domain and tend to deal online, mainly in collectives, stocks and shares.

As you would expect, the SIPP market continues to evolve. Recent developments include SIPP structures that, in essence, operate on a factory gate priced model with the ability to increase cost as you increase the investment sophistication and introduce adviser remuneration. The more sophisticated products offer a genuine whole of market investment choice (without triggering extra wrapper charges) and online access for valuations and administration into the bargain. This has been a particular area of growth over recent times.

### **With a SIPP are you paying for flexibility or functionality that you are not using?**

This depends on the type of SIPP you are using and makes the mistake of assuming that all SIPPs are identical in structure and application of charges. As outlined in the previous section, SIPPs come in all shapes and sizes. The challenge to consider is whether you can match any increase in investment sophistication to increases in the underlying charges.

A case study can be used to clearly demonstrate my point.

Mr Client, male, aged 40 with a transfer value of £100,000 and a plan to retire at age 65.

Using the charges on our own SIPPcentre product as an example, the point should become clear. If I assume that Mr Client is paying a fee direct to his adviser for the advice and I invest initially in the cash fund I am able to isolate and identify the cost of the SIPP wrapper.

Reduction in yield (RIY) is – **0.17%**.

The client and adviser are entirely in control of all investment, benefit and remuneration decisions and hence the total cost. If we look to introduce an element of added investment sophistication or adviser remuneration then we introduce additional cost. If we assume that we want to consider investing in a range of UK exchange traded funds (average TER of 0.35% p.a. and we want to include adviser remuneration of 3% initial plus 0.5% fund based trail there is a natural increase in the RIY.

Reduction in yield (RIY) is – **1.07%**.

If I was to then consider a more sophisticated investment solution e.g. a range of collectives where the average charges are 1% initial plus 1.60% p.a., we again see a natural increase in the RIY.

Reduction in yield (RIY) is – **2.00%**.

Any decision in future to use options such as income drawdown will introduce additional charges. In short, the client will only be paying for flexibility and functionality as it is introduced or used.

There is no doubt that lessons need to be learned from the thematic review. We can be sure that changes can be made to improve the comparability of Personal Pensions and SIPP's. Future success will involve meeting all of these challenges and difficulties head on. Many in the SIPP market remain well placed to do just that. To use another Churchill quote "difficulties mastered are opportunities won".

**END**

**Please note this document is intended for trade and national press individuals.**

**Notes for Editors**

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A J Bell is the UK's largest privately owned SIPP provider and is continuing to grow rapidly in challenging capital markets. Invesco Perpetual and Midas Capital own 23% and 15% respectively of the share capital, the remainder being owned by Andy Bell and the management team.

Established in 1995, A J Bell specialises in providing administration, trustee and actuarial services for SIPP and SSAS.

A J Bell is now one of the largest SIPP trustee and administrators in the UK with in excess of 32,000\* individual SIPP's and assets under administration exceeding £8bn\*. It provides third party SIPP administration services for Barclays Stockbrokers, Halifax Share Dealing, Skandia and E\*Trade.

Recent research by CoreData Research placed SIPPcentre as one of the two most preferred SIPP's.

A J Bell has won an array of prestigious industry awards recognising our reputation for leading products and services. A J Bell products include SIPPcentre, Sippdeal, Sippdealxtra, A J Bell Platinum and A J Bell Securities.

\*As at 30th September 2008.



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