

Article

Turning from a SIPP to a gulp

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SIPPs are increasing in popularity, although the market does now face challenges.

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In his 1989 Budget speech, Nigel Lawson introduced us to the principle of giving individuals control over how they invest their personal pension funds. The first self-invested personal pension was written in the spring of 1990 and in the 18 years since we have seen the market evolve from niche to mainstream. There have been events and outside influences that have affected the pace of evolution. These include the growth in multi-manager pensions, the rise of stakeholder pensions, the demise of stakeholder pensions, A-Day, interest from traditional pension providers and more recently FSA regulation. Two of the most important were the A-Day introduction of the simplified pension regime and subsequent FSA regulation.

Never before have we seen a change in pensions legislation and regulations create so much discussion, debate and press coverage. The debate surrounding residential property pulled Sippis into the mainstream with national and trade press coverage at levels never seen before. The eventual HM Revenue & Customs U-turn was controversial and poorly timed but, all things considered, likely to be for the benefit of the industry over the longer term.

Two years on, some of the arguments of the time have been forgotten. As we look at the possibility of a general election some time between now and June 2010 a few of the old arguments may resurface as part of the political games and competition. In particular, the issues surrounding alternatively secured pension could once again be open for debate.

The view of the government is that:

- 1 Tax relief on contributions and investment growth is provided on the understanding that the savings are used to provide a secure income in retirement.
- 2 Pension assets should not be frittered away leaving the saver relying on the state for the remainder of their life.
- 3 Pension arrangements should not be used as a way for savers to pass assets to their heirs.
- 4 The main way to discourage this is through a penal tax charge on residual alternatively secured pension funds remaining on death of the member and their dependants.

Introducing a tax charge that means the majority face an effective tax rate of 82 per cent is a poorly thought out policy that is not consistent with the stated aim of providing simplicity, flexibility and choice to savers. More importantly, it reduces the likelihood of clients understanding the range of death benefit options available and their associated tax consequences. One thing that can be done is that you could allow payment of any residual alternatively secured funds to any heirs as a lump sum after a one-off standing tax charge. Tax at 55 per cent would act as a neutralising charge to recoup the tax relief previously granted.

Feedback from clients and advisers suggests that feelings still run strong in this area. We intend over the coming months to revisit the arguments for change. Thinking of this reminds me of a favourite saying of an old uncle: "It is true that you do not know what you have got until you lose it. It is also true that you do not know what you have until it arrives."

In terms of regulation, increased popularity and the use of Sippis as a mainstream solution meant that increased interest from the FSA was always likely. Changes would be needed to satisfy the demands of a regulated environment.

The cornerstone of today's Sipp market remains the choice and control of investments available to the client. Regulation meant a greater emphasis on the disclosure of charges, financial promotions and the suitability of advice. This was not something that was feared, more an opportunity to have Sippis sensibly compared alongside the many other pension

choices available to clients and advisers.

The personal pension market now consists of several broad product categories. These include stakeholder, traditional personal pension, multi-manager pensions, platforms and Sipp. The lines between many of these have become a little blurred. However, the different product shapes and the variety of approaches to providing product information can make it difficult to weigh up the pros and cons of the increasing number of available products. Rules on disclosure should enable advisers to accurately compare the costs and benefits of the many products available. The FSA is aware of this and is looking at ways of improving the rules on disclosure.

When it comes to costs, for a fair comparison, advisers and their clients need to consider all costs; which means more than just point of sale establishment and annual administration charges. Also, individual charges must not be compared alone. I received a query recently comparing Sipp companies that applied transfer in charges against some that did not. This was a simplistic comparison that did not allow for the potentially substantial differences that can materialise when you look at all charges.

Many well-established Sipp providers already have transparent products with all charges and adviser remuneration clearly and fairly disclosed. With such a wide range of products available the challenge is to make disclosure more uniform, so a wider comparison covering a range of products is simpler and more robust.

Also, not all Sipp providers provide access to presale illustrations. When illustrations are provided there is often a lack of consistency in how you allow for the cost of the underlying investments. This makes it difficult for advisers to compare products against one another. Where illustrations are provided it is important that they can allow you to build in an allowance for the costs attached to the underlying investments. It may also be helpful to differentiate between the cost of the underlying Sipp wrapper and the costs of the selected investments. This is another area currently under FSA consideration.

The Sipp evolution has already introduced increased competition to an already competitive world. This has created many interesting developments where traditional providers have either launched Sipp or taken the alternative approach and decided to compete head on. As a result, care is needed when considering suggestions or statements, particularly those around price.

In the past some of the biggest mistakes have been made failing to consider the overall effect of charging structures. History shows that it is an easy mistake to make. The market has gone through phases of dismissing highly competitive products simply because they included a charge that had fallen out of favour or because competitors had questioned the use of certain structures.

A simple example will help to explain how easy it is to arrive at false conclusions about different charging structures and price.

Readers will have their own preferences for different charge types. However, like it or not they are all equally good over 25 years irrespective of how much one approach appeals over another. It shows that you need to understand the detail around how charges are applied and you should not assume one is more expensive than the other. Financial advisers need to weigh up recent developments carefully. The pressure on providers to generate profitable success is huge and achieving this means that all sorts of stunts are likely. Future success will involve maximising the good things that this evolution has created while learning from the mistakes of the past. To once again quote my old uncle: "The road to success is always under construction".

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Notes for Editors

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