More to SIPPs

HEADING: **More to Master**

TOPIC: Pensions are dead. Long live pensions.

SYNOPSIS: I had planned in this bulletin to move away from personal pensions and SIPPs and look at some other issues in the wider pensions arena. However in the last few days there has been a lot of comment in the trade press about the likely end of personal pensions – or more correctly regular premium personal pensions. ….

Welcome to this the latest in this monthly series of podcasts and technical bulletins under the title “More to Master”. I am John Moret principal of my own consultancy MoretoSipps – go to www.moretosipps.co.uk for more information.

I had planned in this bulletin to move away from personal pensions and SIPPs and look at some other issues in the wider pensions arena. However in the last few days there has been a lot of comment in the trade press about the likely end of personal pensions – or more correctly regular premium personal pensions. There have also been unconfirmed suggestions that the FSA are planning changes to the capital requirements for SIPP providers. The Financial Ombudsman has also had some things to say about rising complaint levels on SIPPs and personal pensions. So I shall devote this bulletin to considering each of these issues along with some interesting material from Australia on a subject of growing personal interest – the impact of increasing longevity.

But first the future of personal pensions. It’s been reported that luminaries Steve Bee of Paradigm Pensions and Malcolm Kerr of Ernst & Young have both prophesied the end of personal pensions as we know them on the back of auto-enrolment and the move to adviser charging. Now I should first make it clear that I wasn’t in Monte Carlo - more’s the pity - to hear Steve and Malcolm – both of whom I have known for years and for whom I have the highest regard. It’s always dangerous to rely on press reports but there did seem to be some consistency in their message.

Essentially Steve’s argument is that workplace pension reform will drive individuals away from personal pensions into occupational pensions – Malcolm reinforced this by adding in the additional component of the abolition of commission. Neither of these arguments are a surprise – indeed I would add that NEST –if it succeeds – could pose a further threat not least because it will be targeting the self-employed as well as the employed. In my view the regular premium personal pensions market has been in decline for several years. ABI statistics that I have seen are less conclusive but certainly confirm that the rapid growth

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experienced during the early days post-pensions simplification has tailed off.

What we have seen is a steady increase in single premium personal pensions – much of which has been invested in SIPPs. What isn't clear is how much of this is genuine new investment as opposed to the recycling of existing pension investments – an area which has given rise to regulatory concerns. More of that in a moment but coming back to the fundamental point will workplace pensions and NEST effectively eliminate all other forms of individual pension savings? Personally I doubt it unless we also have a change in the pensions tax regime which removes the attractiveness of pensions savings. Indeed as I mentioned in last month's bulletin I think there is every chance that at some point we will see the development of the feeder fund concept – perhaps with the introduction of combined ISA and pensions products and tax limits.

I believe there will always be a place for the individual pension that provides control and ownership – effectively for those in the workplace in the past it was the AVC and today it is the "SIPP on the side". Increasingly those savings are undertaken on a single payment basis rather than with a regular monthly commitment and post 2012 will be operated on a commission free basis. However I cannot at the moment agree with the suggestion that this type of savings vehicle will disappear altogether.

In the last few days Pensions Management magazine has published its excellent annual survey of the SIPP market. This has confirmed that the exceptional growth pattern in this market has continued albeit at a slightly slower rate. My own consultancy MoretoSIPPs regularly compiles its own "survey of surveys" and the most recent has confirmed that there are now over ¾ of a million SIPPs with assets totalling approximately £110 billion. The market is dominated by just five players: Aegon, the AJ Bell group, Hargreaves Lansdown, James Hay and Standard Life who collectively operate over 75% of the SIPPs in existence.

However even in this group there is a huge variation in the average fund size – from just over £50,000 in the case of Hargreaves Lansdown to almost £300,000 in the case of James Hay. This reflects the different target markets and propositions within the overall SIPP marketplace – which become even more diverse when one overlays the new types of drawdown vehicle introduced from April this year. I am convinced that these will over time become a major driver of growth in the SIPP market as it continues to mature with increasing numbers moving into the asset decumulation phase.

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However it's not all good news on the SIPP front. The trade press has covered two stories recently that could damage the growth prospects either for the market overall or for some providers. First there has been speculation that the FSA are planning "to increase the capital adequacy requirement for operators of SIPPs in a bid to protect investors as the products become more popular in the mass market". I have no knowledge as to whether this is correct but as I alluded to in my May bulletin for some time I have believed that the regulatory framework for SIPPs requires a fundamental overhaul. Capital adequacy requirements are only one aspect of this. There are certainly anomalies in the current capital requirements – which some operators have undoubtedly exploited. The big variation in the impact of the FSCS levy on different SIPP operators is another example.

The issue of SIPP regulation was high on the agenda at the recent Association of Member Directed Pension Schemes – known as AMPs – annual conference. This was largely as a result of the recent FSA information request which was sent to around seventy smaller providers at short notice and asked them for a considerable amount of data on topics such as legal structures, regulated activities, use of third parties, regulatory oversight, and a raft of financial and other management information. One of AMPs understandable concerns was the short notice given for the provision of this information. The FSA apparently regard this information request as a follow up to the thematic review of smaller operators that they conducted in 2008.

At the root of all of this is the fact that SIPPs are treated as "packaged products" for regulatory purposes – that was the consequence of the regulatory regime introduced in 2007 as a result of the hysteria created by the prospect of residential property being allowed as a SIPP investment. The fact is that there is a big difference between the SIPPs manufactured by many of the larger providers that only accommodate a limited range of investments and those run by in the main smaller operators that provide much wider investment opportunities – which can come with greater risk. AMPs represents all operators but is heavily influenced by the views of the majority of its members who tend to be the smaller operators. There are believed to be well over 100 SIPP operators – my "survey of surveys" covers 90.

The FSA can only operate within the regulatory regime that exists which means that by and large all SIPPs are treated the same. This approach is convenient and has the merit of consistency of approach – but fails to recognise the difference between the collective type SIPP - often accessed via a platform – and the true bespoke SIPP which can hardly be described as a packaged product. The FSA in their recent consultation paper CP 11/03

recognised this by suggesting a different definition of a SIPP for disclosure purposes –see last month's bulletin for more information. Moreover given that most investments held in a SIPP are themselves regulated investments there does seem to be more than an element of overkill in the current regime. Judging by some of the comments made at the AMPs conference I suspect we've not heard the last of this issue.

The Financial Ombudsman Service has also had something to say about SIPPs if press reports are correct. Specifically they have said: "During the year we continued to see complaints about advice on selecting investments within a pension fund; delays in setting up annuities; taking pension benefits using income draw-down (sometimes known as unsecured pension or pension fund withdrawal); and "switching" (transferring pension funds from one policy to another), particularly into self invested personal pensions (SIPPs)."

At the time of preparing this bulletin I haven't seen any numbers to support these claims but with the growth in the SIPP market it is hardly surprising that complaints may have increased. That isn't any excuse of course but one needs to understand the reasons for the complaints. Interestingly one whole section of the FSA's information request to providers relates to complaints. The concerns around "switching" are real and advisers will hopefully be aware of the FSA's justifiable concerns in this area – and will have proper controls in place over the advice process.

Finally I turn to a subject which is occupying an increasing amount of my time – both from a personal standpoint and commercially – that is the impact of increasing longevity. This is a huge subject which has personal, national and international impacts. It has been described without exaggeration as an issue which potentially will have as big a global impact as climate change. And yet the level of awareness, knowledge and understanding of all the issues – some of which are still emerging – is worryingly low. I am a huge fan of the International Longevity Centre www.ilcuk.org.uk which has and is undertaking a vast amount of research and other activity in this area. I would recommend a visit to their website.

My interest in this subject was partially initiated by unearthing an Australian website www.mylongevity.com.au This site was set up three years ago to provide Australian financial advisers with more information on this subject. At its core the site uses a SHAPE analyser to examine the likely impact of five factors – surroundings, health, attitude, parents - a proxy for our genetic make-up and eating habits. This enables an estimate to be

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made of an individual's likely longevity and the factors influencing it.

When they launched this service in 2008 the average age of a retiring Australian client was 65 and advisers would normally plan on average for a lifespan of around 20 years. This underestimated the real life expectancy by about three years - and since advisers' clients tended to be wealthier than average there was a case for adding on about another two years life expectancy. Consequently in simple terms this amounted to an "underestimate" on average of about 5 years – an error of about 25% which clearly could have dramatic implications on the erosion of wealth.

Recently the site has developed an online training programme for advisers on the subject. It is aimed at Australian financial advisers with the objective of helping them to work with their clients more effectively by taking into account longevity issues. You can find out more via their website – and I would certainly recommend signing up for their free newsletter service on longevity issues. They make fascinating reading.

With the new drawdown regimes starting to have an impact and the introduction of new products such as fixed term annuities a thorough understanding of longevity is going to be all important for advisers with clients approaching, at or post-retirement. I mention once again the new flexible drawdown regime and wonder how many advisers have carried out an assessment of all their current clients to see how many would meet the current MIR for flexible drawdown. This includes clients currently already using drawdown as well as those still to start vesting their accumulated pensions. I remain of the view that where a client meets the MIR there is no reason to delay moving them into flexible drawdown – this can only provide more flexibility than the alternative capped drawdown regime. This of course assumes that the current provider offers flexible drawdown.

Well that's it for this time. I'll be back in around five weeks with the next bulletin – by which time we'll know if we've been lucky in the Olympic lottery, the Derby will have been run, we'll have failed yet again to produce a Wimbledon singles winner and we'll know all the fixtures for next year's football season. Yes there really is more to life than pensions!

I hope you've found this bulletin of interest, If you have any comments or questions you can email me at john@moretosipps.co.uk. As always thanks for listening and I look forward to speaking to you again next month.

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