

The Road to Regulation

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Self-invested personal pensions (SIPPs) became 'regulated' as an investment product in April. The FSA drive for regulation to bring SIPP into the world of packaged pension products – the phrase 'chalk and cheese' come to mind – was to bring these innovative and flexible pension funding schemes within the range of justifying 'suitability' and from that provide them with the authority to judge mis-selling.

As an ex Independent Financial Adviser (IFA) – and for while a compliance officer - I have worked through the reigns of not only the Financial Services Authority (FSA) but also FIMBRA (Financial Intermediaries, Managers and Brokers Regulatory Association), and the PIA (Personal Investment Authority) – and for those older readers NASDIM (National Association of Securities Dealers and Investment Managers) – give yourself a pat on the back if you can remember what that stood for!

The IFA industry has come through some uncomfortable periods – pension review, challenges over endowment mortgages, and the threat of a review of contracted out personal pensions – and add to this regulatory change, in fact that has been the only thing that has been consistent!

So where are the concerns over SIPP and will regulation prevent mis-selling – and as a provider will the volume of extra documentation and procedure changes really make a difference?

Part of the problem has been brought upon the industry by the apparent confusion as to the difference between a personal pension and a SIPP. Somebody in the office the other day asked whether personal pension products still existed! Product providers seem determined to 'blur' the edges – the SIPP is the 'sexy' option but in reality the volume SIPP market is no more than a personal pension with multiple internal and external fund choices.

Are these options that the majority of people saving for retirement need let alone use – and in offering them are we comfortable that the policyholder is not being empowered with too much investment choice? A dangerous mix when there is a lack of understanding of the investment risk – the member is encouraged to monitor and trade investments online – and the input of the IFA post sale is diluted!

So given this confusion we now find ourselves with SIPPs being regulated as a 'packaged product' – we winced when we first read the guidance on cancellation notices – and then we have to tell our clients that we will not establish their SIPP because they might not know what they are doing!

As with many of our peers in this market a SIPP for our client and their advisers is far removed from the personal pension product described above. For us the value to our clients in a true SIPP is to maximise the investment flexibility that the provisions offer and to see the SIPP used by the adviser as a lifetime holistic planning vehicle.

We now have a regulated product that potentially consists of no investment! The basic SIPP consists of an application form and probably at a later date a cheque that is deposited in the member's bank account.

The 'shoehorning' into product regulation might best be served by a recent case study.

A group of individuals in the legal profession have been 'advised' of the merits of purchasing the premises from which the business operates. After further discussion and comment from their professional advisers they all decide to purchase the property through a Trust financially supported by a group SIPP – some 36 members. They all pay different contributions and borrow different amounts to complete the purchase.

At no point in this process, or since, has any member purchased a regulated investment product – save now of course for the 'wrapper' they needed to create to purchase the property. These individuals were going to buy the property in any event but decided to do so using the group SIPP concept for reasons of tax benefits. I do not doubt that consideration needed to be given to both the pros and cons of such a route but such individuals – with the benefit of high quality independent

advice, which such clients will always have – are not viewing their SIPP in the way that you and I might as their main investment vehicle for their old age!

In fact they all have an individual SIPP or personal pension that they view as their 'pension fund'.

It is quite correct that the would be member receives product information such as the Key Features Document and as best we can ensure they make an informed decision but in this sector of the market the level of financial knowledge is above average and such individuals invariably benefit from external professional advice – for which they pay substantial fees.

Previously of course the regulatory compliance procedures sat around the subsequent advice as to where this money was to be invested and the development of an investment portfolio that matched the member's attitude to investment risk. These requirements remain in place anyway both at inception and for subsequent reviews.

There are certain lessons that we should learn from previous examples of legislative change.

First, the industry will make the required changes to both internal and external procedures. There is no doubt that for some the regulations will result in a review and subsequent improvement of controls – particularly financial.

These changes will result in an increased cost of trading and the question will then be whether for some this can be reflected in a cost to the consumer. In my opinion these costs will have to be absorbed by the provider given that the market prices for SIPP have been continuously driven down over recent years on the back of e-commerce and to some extent a fear factor of loss of market share.

For the provider of a true SIPP in a non-volume market there is a real danger that we over-estimate the importance of price. As long as the administrator's fee is sensible, does the member really make decisions on costs that are so insignificant in relation to the added value of the product and the service the provider brings to the relationship?

I believe there is a real risk of being 'cheap' – what worth the customer who knows the price of everything but the value of nothing!

If increased costs cannot be absorbed then the history of regulation shows that the market consolidates. These are early days and we will have to see how some providers manage over the next 24 months but there must be the prospect of mergers and takeovers especially with the continued market expansion and the resulting pressures on service levels and systems investment.

I am not so sure that consolidation in such a specialist financial planning arena is necessarily a good thing for those individuals who are affected.

The second consequence of legislation is the increased volume of pre and post sale material! It has been commented that following the regulation of mortgages there are now another 12 pieces of literature that go to the consumer!

But will anything that we will now produce as a specialist non-volume SIPP provider make any difference to the risk of one of our products being mis-sold in the market with which we are familiar? The answer is of course an emphatic – no!

In fact we are more likely to get complaints from the applicant for questioning that they might not know what they are doing!

So as we adapt to regulation and look forward to a continued growth in this 'new world' of pensions what early conclusions can we draw on regulation?

- Regulation of a SIPP will not prevent mis-selling – the role of a good IFA is to determine the suitability of various products for retirement planning – stakeholder, personal pension with multiple fund choice or then a true SIPP – the latter is not a volume market product and should be focused towards those that are more readily equipped to reach informed financial decisions.

- The SIPP provider industry will face increased costs in adapting to regulation; whilst this will have a benefit in strengthening internal procedures and financial and business governance these costs will put pressure on product pricing. The risk is that where this cannot be passed on to the member there will be consolidation in the market that might result in some good firms losing their identity and clients being unwilling victims of corporate change – not always matched by service improvement.
- As a SIPP provider we will produce more support material for the adviser and their client both pre and post sale but this will not prevent mis-selling. For our market the material will be bordering on the irrelevant with the real regulation continuing to be appropriate for the selection of investment products to be held within the SIPP.

The trouble is we are now on the journey and there is no end. I am opening up a sweepstake here in the office on the number of FSA consultation papers we will face in the next 12 months!

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