26th JULY 2013

Welcome to TISAtalk, this week –

- Malcolm Small, Director of Policy at TISA, outlines why the pensions market needs to rethink its approach to annuities.
- Jeffrey Mushens, Technical Director at TISA, provides an update on the Client Assets Best Practice Project and why the recently announced FCA consultation on this topic fits in well with the work the Project Group are involved in.
- Peter Smith, Head of Distribution Engagement at TISA, discusses how new capital adequacy requirements and the Sipp thematic review has triggered consolidation and takeovers.

THE TROUBLE WITH ANNUITIES…

In all my years of conducting consumer research around pensions, there is one area that always seems to get interviewees really angry when they start to understand how they work, and that is annuities. Many consumers do not understand that they will have to pay income tax on their pension income, and fewer still understand that, for the most part, they will be shoe-horned into buying an annuity, certainly if they do not take financial advice. They find the concept of giving their money to an insurance company infuriating and the concept that their money will die with them incomprehensible. I have some very real anger emerge during interviews and focus group sessions when annuities, and how they work, are explained.

Why does this matter? Because, as the baby boomers move towards retirement, there will be a wall of money coming to the market to produce income. As an industry, we have largely been focussed on the accumulation of assets which we can then manage for growth. Soon, the emphasis will be on managing instead for income, whether through an annuity or through income "drawdown" direct from the pension fund. Empirically, this latter option would seem to be the soundest approach, as with the prospect of a 30 year "retirement" for more and more people, exposure to the markets would seem wise. Yet income drawdown as currently constructed is not without its technical drawbacks and the collective investment industry has been curiously slow in constructing funds dedicated to producing reliable and sustainable income streams.

Policymakers and the industry need to listen to the legitimate needs and expectations of consumers in this market, and react to them. The baby boomers' lives are not going to be as linear as the lives of retirees 30 years ago, and an annuity is a very "linear" product in the income streams produced. We need to start re-thinking retirement income.

Malcolm Small, Director of Policy

UPDATE ON CLIENT ASSETS BEST PRACTICE PROJECT

The FCA announced a consultation on Client Assets on Friday 12th July. This fits in well with the work our Client Money Best Practice Working Group is undertaking developing statements of good practice for members in areas where the existing rules are unclear.

The FCA is interested in the output from this working group. We had a good discussion with them on Tuesday, where we updated them on the investigations and tasks undertaken so far, and sent them our questions on CMAR. Next up for debate within the Working Group is 'Interest'. There's a lot for TISA members to read in the CP, and the FCA said they're likely to respond to our request for a Q&A session with them in September, ahead of the close of the consultation.

TISA believes that development of good practice is helpful for our members, the industry as a whole and for FCA. Not as an additional form of regulation, but as an industry guide that the FCA can point to, that provides useful direction for members.

The FCA can never be as close to the detail as industry practitioners, who generally just want to comply fully and accurately. Helping them do so in a consistent way will be a good outcome of TISA's work.

Information on the consultation can be found at the FCA website via the link below.

http://www.fca.org.uk/your-fca/documents/consultation-papers/cp13-5)

Jeffrey Mushens, Technical Director

SHOP UNTIL YOU DROP

Some shopping sprees are exciting and somewhat rewarding depending on the location and the amount of cash in your pocket, to others they spread fear and trepidation at the thought of spending valuable money.

That is exactly what has been happening slowly for some time in the Sipp market, and this is gathering pace.

Sipps are over 20 years old in concept and it could be said the market is now maturing, but current developments seem to indicate it is still in the growth stage for certain practitioners. There are large-scale takeovers and multi-million pound deals being completed, whilst consolidation has been increasing since Legal and General acquired Suffolk Life in 2008. The driver for accelerated growth follows the FCA proposals, originally under the FSA, to increase the capital adequacy minimum capital requirement from £5,000 to £20,000.

This is a pivotal point, when you consider the creation of the original Sipp product and its intention to accommodate non-standard investments. The changes to the rules are anticipated in the second half of 2014, and have triggered a spate of acquisitions, with Suffolk Life going on to purchase books of business from Tenon, Pointon York and more recently those of Origen. In the last year the Sipp books of Lighthouse, Montpelier, BNP, Alliance Trust, Equiniti and Ashcourt Rowan have all changed hands.

The two main drivers here are the new capital adequacy requirements and the Sipp thematic review which has handed out some serious challenges to Sipp operators around regulatory requirements, oversight and management of operational risk. The review found a number of Sipp operators were holding insufficient capital to absorb unexpected liabilities, and risk in the ongoing viability of the firm. There was also evidence of conflicts of interest existing within some operators acting as the administrator, trustee and adviser with indications there were insufficient controls in place to manage potential conflicts.

There has been a significant increase in unregulated investments in some Sipp providers with scant control to check the investment assets are suitable. There also still needs to be a clear indication of scheme liability checks even if the Sipp operator is not actually dealing in them.

From the seller's perspective it is not hard to understand why they are keen to put up the summer sale signs. For a number of the firms their core specialism is advice and currently it is tough enough running an advisory business without running a complex administration business alongside it, not to mention the increased capital adequacy requirement draining a business that probably doesn't have scale and indeed the right level of management to cope with the requirements. In addition, the recent platform paper forces those Sipps on platforms to unbundle charges and demonstrate a payment by the investor not the fund manager, which adds an additional element to pricing transparency.

For those with ready cash looking to purchase Sipp books, the trend so far has involved well capitalised higher end providers purchasing individual Sipp books, cherry picking the segmented books that they want. Most people will want to ensure they purchase a clean book of business with the right kind of investments with proper records and documentation so that they are not involved in lots of back office work and investment cost.

The buyer beware sign is brought into focus with the capital adequacy requirements on non-standard assets. There will be a number of toxic books which may remain on the market unwanted by any acquirer. Schemes with Ucis or access to pension liberation schemes would need to be given some sort of guarantee by the FCA and HMRC, before anyone will go near. It will be interesting to see how any investors stranded in such toxic books are protected or rescued by the new regulator.

My view is that the Sipp bazaar is likely to see money changing hands for some while.

Peter Smith, Head of Distribution Engagement

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