Welcome to TISAtalk, this week –

- Malcolm Small, Director of Policy at TISA, discusses the debate on pension scheme charges being low to the detriment of the businesses proving the products or high to the detriment of the consumer.

- Jeffrey Mushens, Technical Director at TISA, outlines why the financial services industry can sometimes suffer when government gets involved, citing FATCA and CTFs as examples.

- Peter Smith, Head of Distribution Engagement at TISA, discusses the impact of a cap on consultancy charging for auto-enrolment advice

RIP-OFF CHARGES – MYTH OR REALITY?

Perhaps it's the silly season, with little fresh news around, but the debate around pension scheme charges has been back in the headlines this week. Much of the industry has kicked back on this issue claiming that, since the introduction of stakeholder pensions and the effective 'capping' of charges at 1%, the matter is a dead duck. To an extent this is true, and with the latest initiative of automatic enrolment and the establishment of the National Employment Savings Trust (NEST), further pressure has been brought to bear on price. The new 'price point' has been pioneered at just 50 basis points 'all in' by organisations such as The People's Pension and NOW! Pensions, although details differ. This augurs well for the future. It is important that as little as possible of a pension fund is eaten by charges.

However, the charge for the pension 'wrapper' itself is just one part of the picture in a typical legacy stakeholder scheme. Charges for 'active' investment management are on top, as are any advice charges. The investment element can see an annual management charge of another 1% typically, with a total expense ratio of another 1% or more. This is a much less rosy picture. Even so, I was recently asked to look at a scheme to see whether it might be suitable to be used as an auto-enrolment vehicle. I was confronted by a contracted-out 'money purchase' scheme from the late 1980s with charging features which today would make your hair stand on end, such as 'capital units' (remember them?) and 'bid/offer spreads' of 5% on the funds. All normal practice 25 years ago, but not a place we would want to go back to.

My concern is that the pendulum may be swinging too far the wrong way on charges. I have been in the fortunate position of being able to look into quite a number of business plans for current market participants. I recall that, at the time of stakeholder pensions, providers were openly talking about 'breaking even' in 12 or 15 years, never mind showing a double-digit return on capital. At the time, I thought this was the economics of the madhouse – and I still do today. There is little point in super-low charges if your pension scheme goes out of business.

Malcolm Small, Director of Policy

PUT NOT YOUR TRUST IN PRINCES

I've been thinking about this term in the light of two recent events.

The first was the announcement by the US IRS that FATCA was being put back another six months. For months the industry had been assured that the FATCA registration portal would open on time in July, despite the sceptics doubting this would be the case where governments don't have particularly excellent records in delivering time critical complex IT solutions in short time frames. Regardless of the US having signed an IGA with the UK, the first HMRC knew of this - in breach of the IGA - was an email in their inbox.

This has been infuriating for everybody concerned. If the industry had known at the start the final shape of the IGA and the critical dates, it could have delivered a more efficient and less costly solution. As it is, the industry has to bear more delays and uncertainty.

The second is the recent consultation on Child Trust Funds to which TISA (representing CTF, JISA and ISA providers) responded. We liked the original idea of the CTF. It would give everyone a financial stake in society and would be a perfect tool to get students to engage in personal financial education. After all, it's much easier to engage students' attention about financial education when they have money in the system.

The industry trusted the government's ongoing commitment to CTFs so spent millions on systems and involved government in product design. So when the current government, facing a terrible financial legacy, changed the rules those who trusted them felt betrayed.

The lessons I draw here is that government shouldn't get involved in detailed product design. They can't be trusted not to change the rules after the event and are too prone to listen to vested interests.

Jeffrey Mushens, Technical Director

OUT OF TIME

Certain things often develop rapidly without you noticing. Monday 17th June saw the second reading of the new pension bill which ushered in a single tier state scheme and mass membership for auto-enrolment as part of the government's strategy to revolutionise pension provision for non-savers. This bill will also contain confirmation on the abolishment of consultancy charging with effect from 10th May and confirming that advisers are unable to operate the practice on new schemes from now on. However, a number of advisers and benefit consultants may not detect that regulations are in the pipeline to extend this to all qualifying auto-enrolment schemes. The government is in effect changing the dynamics for employers to now clearly *buy advice* and not have the charges spread across members' pension pots.

This move has wrong-footed many pension providers and consultancy strategy teams with the DWP's announcement of an immediate ban. Market chatter is that certain providers have had to abandon many pounds' worth of systems development within weeks of its implementation. The direction of travel is now clearly marked from both the DWP and OFT, and had been indicated for some time.

So what of the future? There is an indication that a consultation on a charges cap will commence this autumn. Right now, the consultancy charging ban has had little retrospective impact on current schemes as probably only a few have been set up on this basis.

The bigger threat for employers and advisory businesses is that the charges cap will apply to all auto-enrolment schemes. This will include a large number of the buoyant group personal pension sales of 2012, with many still currently being implemented, driven by the 'buy now while stocks last' commission drive of corporate advisers. The concern is very much around the impact of commission payments on the annual management charge, which could disqualify some of these group personal pensions as qualifying workplace schemes. If there is a benchmark of the annual management charge set at 0.5% ,which interestingly the DWP calls the baseline level, this may well force commission-based schemes to comply with or explain their charges. This could have an impact for employers who have purchased auto-enrolment ready schemes with commission payment as a mechanism for the implementation and employee communications functions.

Advisers and employers will have to explain to new employees whose pot will be following them, how the charges operate and why the charges on their existing pot as well as future pots have just gone up. There is a danger for both employer and adviser to be running a large reputational risk here. For those advisers and employers looking to certify schemes as qualifying for auto-enrolment, their existing GPP will need to consider how such schemes will be amended and explained to staff.

Peter Smith, Head of Distribution Engagement