The long and the short of SIPPs

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This month, Ray Chinn focuses on the quality of information provided by SIPP providers and whether this is sufficient in setting realistic expectations for customers.

Q. The FSA have recently commented regarding the disclosure of charges under SIPPs. What is all the fuss about?

Ray: The short answer: The FSA are concerned that customers are not being provided with the right information to make an informed decision about the product they are purchasing. Broadly speaking these concerns focus on the disclosure of charges.

The long answer: The issue relating to disclosure of charges under SIPPs has been a hot topic for some time. Lack of clarity about the interest element of bank account balances which SIPP providers may or may not be passing on to the customer is often viewed as 'public enemy #1' in this respect. In the recent review of small SIPP providers the FSA was again critical in this area and explained exactly what they expected to see in terms of disclosure of any retained interest. The report also highlighted that any 'commissions' from investments retained by providers should also be clearly disclosed.

If this is taken to the extreme this could mean that rebates for fund management which are often paid to SIPP providers, or other platforms for that matter, should be disclosed. This would lead to much more transparency in terms of what the actual charges being paid are contributing towards.

For example if a SIPP provider receives a 'rebate' of 75bps on an OEIC fund but still charges the customer 150bps it will effectively be accruing 75bps itself as income. If I were being cynical I could suggest that the apparent 'free' SIPPs are using this facility as a marketing ploy and not being completely open and honest with customers. A more transparent and RDR friendly approach would be to show investments on a 'net of rebates' basis – which some SIPP providers, including LV=, are now doing. Top selling retail OEICs @ 75bps anyone?

The other area which has attracted some critical comment is in terms of SIPP fee menus. It could be argued they do not provide a clear indication of total charges that may be levied – for example how many investors know how exactly how many transactions, at £25 each, they are likely to undertake during a year? The FSA also pointed out some firms quoting 'time cost' charges - say £300 per hour, without quantifying this in terms of how many hours work a specific transaction may take. Hardly TCF.

Q. Projection rates on illustrations have also been identified by the FSA as requiring attention, what is the issue here?

Ray: The short answer: The short answer: FSA rules require providers to supply illustrations of future benefits on realistic rates of return, rather than simply using the standard 5%/7%/9% p.a. rates. Many providers are ignoring them!

The long answer: Whilst no-one would condone using over optimistic projection rates – we should be aiming to make customer expectation of outcomes as realistic as possible – the industry has generally struggled with this concept.

Some providers have defended using higher growth rates for cash based investments on the basis that these investments are likely to be 'switched' into equity backed assets for the majority of the investment period. The challenge here is when the provider uses equity style growth rates with cash type charges!

For those providers who have moved to realistic growth rates in line with the FSA rules (my own company is one of the few), we find that this leaves us in an unfair competitive position where other companies are flouting the rules. Even where realistic projections are being quoted, different providers will use different rates making comparisons virtually impossible.

There is a clear opportunity here for one or more of the industry trade bodies to take the lead and work with the FSA and the industry to come up with growth rates that are both realistic and provide a 'standard' basis to enable product comparisons to be made. To date, the ABIs sole input into this debate seems to have been a rather lame reminder to it's members of the need to use realistic projection rates - with little noticeable impact!

Advisers should look at illustrations carefully to ensure they fully understand what is being considered and that this is appropriate, allowing the customer to make an informed choice and on the basis of sensible information.

What are you experience of SIPP providers and how they disclose charges and produce meaningful illustrations (or not) for customers?

Come and have your say online at 'Ray's Chinn-wag' www.ifaonline.co.uk/tag/chinn-wag where the debate continues…

Next month – Ray will be continuing the debate on charge disclosure, and picking up on issues raised online.