



WHY CAPITAL ADEQUACY SHOULD BE AT THE TOP OF EVERY ADVISER'S LIST OF DUE DILIGENCE QUESTIONS FOR SIPP PROVIDERS

Self-invested personal pension schemes (SIPPs) have been acclaimed as the leading success story for the last decade with double-digit growth rates. However, closer inspection sadly reveals industry-wide mis-selling and malpractice.

At present it is quite confusing for IFAs, as there is a plethora of different SIPP products in the marketplace with a varying number of providers with different capabilities and cost structures. It is often the case that IFAs compare 'apples with oranges' when looking at the cost of one SIPP provider against another.

THE COMPLIANCE ANGLE

The publication of the Financial Conduct Authority's (FCA) thematic review of the SIPP sector highlights inadequate risk processes, poor quality management information, an increase in the number of non-standard investments held by some operators, and inadequate due diligence being undertaken for introducers and investments. Therefore, IFAs should consider focusing more on the impact of the new capital adequacy rules rather than the product itself.

From 1 September 2016, the FCA will introduce a number of changes to the existing rules. These will have a significant impact on SIPP providers, especially those that have focused heavily on the non-standard market, and have a high number of clients in that category. The changes will be:

- The capital requirement calculation will be based on the average assets under administration value over the last four-quarter ends, rather than one set point in time
- The initial capital requirement factor will vary depending on portfolio size
- A standard assets list has been defined
- There will be changes to the capital surcharge calculation and formula

WHAT DUE DILIGENCE QUESTIONS SHOULD I BE ASKING MY SIPP PROVIDER?

Providers are trusted with clients' assets and they should take that responsibility seriously. There are a number of questions IFAs need to now be asking their providers in order to safeguard their clients' interests:

- What is the basis of your capital adequacy calculations and what actual level do you hold?
- How do you intend to meet the new capital adequacy requirements?
- How do you make sure you meet the FCA's expectations on non-standard investment due diligence?
- Does your firm hold professional indemnity insurance?
- Has your firm been part of the FCA thematic review?
- Has the FCA placed any restrictions on your business and the investments it can accept?

The FCA recently sent a warning letter to all SIPP operators stating that a significant number were failing to comply with capital requirements or undertaking inadequate due diligence in relation to 'non-standard' SIPP investments.

With numerous SIPP providers already trading on thin margins, many may not be able to comply with the new requirements. Some SIPP providers will exit the market and leave clients' pension savings at risk. In order to stay solvent, others will need to dramatically increase scheme fees. The industry now needs to instil a strong compliance culture to protect clients' assets and demonstrate that it can regulate itself in line with FCA expectations.

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