

Talking points – Financial Services Compensation Scheme (FSCS)

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This factsheet is intended for information purposes only. Its contents are not to be used as legal, financial or tax advice. The tax treatment and tax benefits are based on our understanding of current tax legislation.

The different types of SIPPs and the assets held within them frequently give rise to questions over how the FSCS applies to them.

In this Talking Points we explain the differences between types of SIPP and investments, and how any potential claim could be treated.

The FSCS only covers firms that are authorised by the Financial Services Authority – all SIPP providers since 2007 - referred to as operators on the FSA legislation must be authorised.

Types of scheme

Generally SIPPs are established in one of two ways:

- » As a contract of insurance under a Deed Poll
- » Under a trust, usually a Master Trust, covering all investors although each investor may be a joint trustee along with the corporate trustee.

Deed poll scheme

Each plan is established as an individual contract of insurance, issued by a life assurance company. The life assurance company is usually the scheme operator and will be authorised and regulated by the Financial Services Authority. Investors will each receive an individual policy.

The insurance company is the legal and beneficial owner of the assets.

Generally VAT will not be chargeable on the SIPP fees

Master Trust scheme

Investors become members of the scheme, and are generally issued with a membership certificate. The trustee(s) is/are the legal owner of the assets with the member as the beneficiary. Where the member is a co-trustee they will be required to be a co-signatory on the bank account and when making other investments.

VAT will be chargeable on the SIPP fees

SIPP operator defaults

Assets held in a contract of insurance are assets of the insurance company and hence are covered up to 90% of the claim with no upper limit from January 2010.

Assets held under Trust are held by the trustees and hence are not assets of the SIPP operator. The protection may therefore be significantly lower, with FSCS compensation limited to £50,000 as at January 2010.

Underlying assets

Where the custodian or provider of the underlying assets fails then the SIPP operator or trustee can potentially claim against the FSCS on behalf of the scheme member.

The level of compensation payable depends on the status of the custodian or provider, the nature of the investment and the eligibility under the FSCS.

Deposit accounts

The SIPP trustee or operator should be able to claim under the FSCS for each investor involved. For example, we have for both our deed poll scheme, the Suffolk Life SIPP and the master trust scheme, the Suffolk Life MasterSIPP, successfully claimed and recovered the maximum for each investor involved when the Icelandic Banks collapsed. The limit is £50,000 per individual investor.

Insurance based investments

For funds issued under a contract of insurance, the insurance claim limits would apply. That is, 90% of the claim with no upper cap as at January 2010.

Other investments

If the firm providing the investment is regulated by the FSA then the level of potential claim is up to £50,000.

If the investment firm providing the investments is not regulated by the FSA, then no claim can be made against the FSCS. For investments provided by European firms who are regulated by their home state regulator the SIPP operator and trustee *may* be able to claim but this is not certain.

Our view

To understand how FSCS protection relates to SIPPs, one must first establish the legal structure of SIPP scheme. Then it will be necessary to determine whether the claim would be against the operator of the SIPP or against the provider(s) of the underlying investment(s).

FSCS continued

The level of investor protection offered to SIPP investors will depend on the way the SIPP is established and its legal structure. Unfortunately currently there is no correlation of compensation arrangements with the FSA's capital requirements. This has led to different providers adopting a range of legal structures in some cases to minimise the capital requirements – for example by electing not to hold client money.

Given the importance to investors of compensation arrangements its important that advisers fully understand the legal structure of any SIPP operator that they do business with – and also fully appreciate the potential implications and impact on compensation arrangements.