Cross-selling opportunities and the chance to catch customers at a very early age may persuade financial institutions to offer the Government's new child trust funds, writes Michelle Perry.

child's pay

Few UK consumers will live long enough to switch bank accounts, according to the latest research by the Bank of England (BoE). The BoE study of the UK current account market concludes that the average account holder would take 91 years to switch. With this knowledge, it's hard to see why so few financial institutions have publicly pledged to offer the Government's new child trust funds (CTFs).

In 2002, there were 596,122 births in the UK, an increase of 0.25% on the previous year. If birth rates continue to grow at the same pace then banks, building societies and insurance companies are potentially looking at a massive number of new account holders on a yearly basis who will remain loyal customers for the duration of their increasingly long lives. But despite the launch of the mandatory new savings products from the Government, only two providers have come forward so far.

Under plans first announced back in 2001, families of every child born after 1 September 2002 will receive a one-off voucher of £250, with a further payment when they reach the age of seven, to invest in a tax-free CTF. Poorer families will get £500. Family and friends will be able to contribute up to £1,200 a year between them into the fund.

Financial institutions reluctant to commit

But despite the first funds being made available in April 2005, only Fidelity and Norwich Union, in a tie up with friendly society, The Children's Mutual, have made firm commitments to launch CTFs in 2005. Scottish Widows has in principle agreed to offer the fund, but will not commit until clear guidelines are finalised. A spokeswoman said: 'We are looking to offer it but until we have more details we can't say how or what we'll be offering.'

It is here that the problem lies. With less than a year to go before the Government issues its first round of vouchers, the rules and sales regime still hasn't been finalised. Tony Herbert, policy adviser at the Association of British Insurers, says: 'The picture of who is offering CTFs is still murky. The Financial Services Authority (FSA) has only just published details on the sales regime so even though organisations had an idea of what it would be like, many haven't wanted to commit before knowing the full picture.'

Many institutions will be unable to provide the funds

The biggest points of contention centre around who can provide the funds and the price capping structure. There are two types of CTF, stakeholder and non-stakeholder. The stakeholder product will be an equity-based product with statutory minimum standards. Non-stakeholder CTFs will be subject, for the most part, to existing regulatory requirements.

Here's the rub: all providers must be able to offer both products in order to qualify under government rules. Under the current proposals, many credit unions and building societies will not be able to become providers, because they are not regulated by the FSA, the watchdog that will oversee the sales regime. Excluding these financial institutions, most of which are well established and trusted among local communities, could, say experts, defeat the Government's aim of nurturing a savings culture for all.

Increasing the number of providers

The Inland Revenue has made some concessions to widen the scope of providers by allowing credit unions and building societies not regulated by the FSA to become 'introducers'. But the Building Societies Association (BSA) is indignant. The BSA claims it will restrict consumer choice and may drive consumers towards 'riskier, equity-based products, when they may prefer the

capital-certainty of deposit-based products'. The Association points out that building societies are traditionally the natural place for parents to go to when considering where to open a child's account. But the Government is working on the supposition that equity products outperform cash-based deposits over the long term, allowing CTFs to grow at a faster rate.

Under the existing rules, 17 building societies, more than a quarter of the sector, will not be able to offer the CTF. Although the societies are now able to 'introduce' the fund through a third party if they cannot provide it themselves, a spokesperson for the BSA says the industry feels forced into a corner over the issue. 'The question is can they afford to offer the equity product and should they have to? The cost of getting permission from the FSA, but also the resulting costs in compliance and staffing issues, are holding them back, especially when they already have appropriate products for children,' says the spokesperson.

The same obstacles are preventing credit unions from launching CTFs. Ciara Morrison, policy officer at Abcul, the credit unions' association, says: 'Roughly 20 credit unions are interested ranging from the largest down. But I'm not sure of their interest if they can only be introducers. There's a lot of hoops to jump through.'

Abcul CEO Shaun Spiers, says: 'The FSA has been very responsive to our concerns about credit unions' possible total exclusion from this market. We are therefore continuing our search for a provider, which will accept introductions from all credit unions with the necessary permissions. It will be a great shame if they are not able to offer their members the child trust fund.'

The price cap

The other point that has delayed many organisations is the price cap. Initially the Government planned to set the price cap at 1%, but this was met with staunch resistance from finance firms. They argued that the 1% charge would not work on stakeholder schemes because the operating costs would mean there was little profit to be made.

The Government has since conceded and raised the price cap to 1.5%. The industry still isn't satisfied with the cap, but will tolerate it because it's a mandatory product. Experts say, however, that it's a moot point whether CTFs will raise cash. Samantha Mitchell, director at the British Bankers' Association, which represents 240 member banks, says: 'In principle they don't agree with price capping. They believe in transparency in setting fees. But it's a mandatory product so it's up to the organisations if they want to offer it under these terms.'

Cross-selling opportunities

Despite continued wrangling, experts believe many more organisations will offer CTFs because of the potential for cross-selling to parents and relatives and the continued evidence that once you're with a bank, the likelihood of switching is minimal.

Herbert says: 'Over the coming months we'll hear more about providers. I wouldn't be surprised if we see more tie-ups with supermarkets and children's stores.' He adds: 'If you have a customer at that early age and you have access to their parents there's the prospect of cross-selling.'

Those organisations with well developed branch networks are believed to be the ones that will be best placed to sell the products. Herbert says: 'It's practically easier to visit a local branch. You get a pack sent out if your child is entitled to a voucher, but if you're not sure then you might end up on the high street at the local bank or building society.'

Ultimately it is up to the organisations if they choose to provide CTFs. Many are still weighing up costs versus opportunities. It will, in the end, be the issue of cross selling and retaining customers from birth that will make the decision for most institutions that are still wavering. ■

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