the Money Advice Service™

Consultation response

Creating a secondary annuities market

Response from
the Money Advice Service

June 2015

About us

The Money Advice Service is a UK-wide, independent service set up by government to improve people's financial well-being. Our free and impartial money advice is available online and by phone, web-chat or face to face with one of our Money Advisers. We also work with the debt advice sector to fund and to improve the quality, consistency and availability of debt advice.

Our core statutory objectives, as set out in the Financial Services Act 2012, are to enhance the understanding and knowledge of members of the public about financial matters (including the UK financial system) and to enhance the ability of members of the public to manage their own financial affairs. We work closely with others to achieve this. The Money Advice Service is paid for by a statutory levy on the financial services industry, raised through the Financial Conduct Authority.

We are responding to this consultation in light of our statutory objectives and our wider role to ensure that consumers are well informed and empowered to take action across the existing and emerging retail financial services marketplace.

Executive summary

We recognise the complexity of creating a secondary market for annuities and welcome the opportunity to contribute to the secondary annuity market consultation.

There is also the wider need to improve the financial capability of consumers across all of pensions and retirement income and also more generally across all money matters. This can only be tackled through a broader set of actions, which brings together partners across the whole industry to focus on improving general financial capability in the UK. The Money Advice Service is working with stakeholders across financial services, government and the third sector to develop a UK financial capability strategy, which will be published later in 2015.

With the current pension reforms, the challenge remains to break down the barriers for consumers, by making personal information about their pensions more accessible, using consistent language across the industry and statements and projections that are easily digestible. However, we also know that good information is not enough to change behaviours and that financial capability, good regulation and market competition have a significant role to play.

All of these challenges remain when considering the creation of the annuity secondary market. Consumers need to have access to regulated financial advice and guidance to be able to discern good decisions from poor decisions for their annuity assignment.

The Money Advice Service welcomes the opportunity to participate in further work to create good consumer outcomes.

Response

Our response addresses question 1-8, and 10-17.

Question 1. In what circumstances do you think it would be appropriate to assign one's rights to their annuity income?

There are limited circumstances where one's rights to their annuity income should be assigned to a third party. If an individual has suitable secure income and the annuity income is surplus it may be appropriate. A suitable income test could be implemented to prove a sufficient level of income from other sources. This notion is akin to the old flexible access drawdown income requirements of £12,000. This would ensure the customer is not giving up a much needed source of secure income.

Another circumstance may be if the health of the annuity holder has declined significantly to drastically shorten life expectancy; the holder may wish to sell and use the lump sum to meet other pressing needs. It may also be appropriate if the current annuity is not suitable to provide for a surviving spouse (i.e. single annuity was purchased when joint annuity would have been more suitable).

Question 2. Do you agree with the government's proposed approach of allowing a wide range of corporate entities to purchase annuity income in order to allow a wide market to develop, whilst restricting retail investment due to the complexity of the product? What entities should be permitted and not permitted to purchase annuity income and why?

MAS agrees that direct retail investment should not be permitted, as the complexity of the products may create unacceptable misselling risks.

It is difficult to form a clear view of the Government's proposed approach in the absence of a detailed assessment of the types of corporate entity which may participate in the new market. It is possible that, since the decision to implement this change is scheduled for April 2016, an annuity holder wanting to sell their annuity on the first day of the new freedom may have a very limited market in which to do so. It may not be competitive if only a very small number of providers are willing to take on annuity assignments, with attendant risks for consumers (i.e. annuitants).

Question 3. Do you agree that the government should not allow annuity holders to access the value of their annuity by agreeing to terminate their annuity contract with their existing annuity provider ('buy back')? If you think 'buy back' should be permitted, how should the risks set out in Chapter 2 be managed?

Currently, consumers have a difficult time shopping around for annuity products. It is a complex market with many barriers that lead to a disjointed and confusing customer journey. Due to these factors, many consumers stick with their existing provider as it is easier and is not considered to be worth the extra retirement income to buy from a provider that the individual has no existing relationship with.

With the current market in mind, we agree at this stage "buy-back" should not be permitted with their existing providers. The "buy-back" concept would also depend on the advice aspect of this new reform. If advice is sought from a financial advisor then it may be the best recommendation to go with the customer's existing provider. Another solution for "buy-back" as put forward by the industry is a blind bidding process. This process would by-pass the shopping around problems and present the best market solution for the consumer.

Question 4. Do you agree that the solution to the death notification issue is best resolved by market participants? Is there more the government should be doing to help address this issue?

This issue should not be resolved by the market participants. This may lead to fragmented notification requirements which may prove difficult to enforce.

The responsibility of death notification should not fall to the estate of the original annuitant. The annuitant may not have a will or have not updated their current will to reflect the annuity assignment. The expense of creating or changing a will to accommodate an annuity death notification clause would become the cost of the annuitant. It represents an unnecessary cost burden to the seller.

One solution may be for providers to check the death registry against their annuity records. All deaths in the UK must be registered so it would provide accurate information for the provider to use.

Further analysis of how the death notification system in the UK could support this requirement is needed. The liability or cost of death notification should not be transferred to the original annuitant or become the responsibility of their estate.

Question 5. Do you agree with the proposed approach of the government working with the FCA regarding the fees and charges imposed by annuity providers?

The current government proposal to monitor the fees and charges of this new market is unclear. As stated in the consultation document, there is a risk that annuity providers may charge excessively high fees since it has the power to deny the assignment. There are current discussions about high exit fees for pension pot transfers when consumers want to access a pension freedom from another provider and MAS notes that a consultation is forthcoming. MAS initial view is that the FCA should lead on the fees and charges as they regulate the market.

Question 6. Do you agree that the scope of this measure should be annuities in the name of the annuity holder and held outside an occupational pension scheme?

Many annuitants will not understand whether their annuity is held inside or outside of their occupational pension scheme. So in theory, the reforms should be extended to all annuity holders as the pension freedoms exist to support all defined contribution scheme owners. It would be inequitable to only extend the freedom to some annuitants.

We appreciate this may affect the occupational pension scheme when the annuity is held as an asset and may have a detrimental impact to the health of the scheme.

Question 7. Are there any other types of products to which it would it be appropriate for the Government to extend these reforms?

MAS is not aware of any current evidence to support extending these reforms to other products.

Question 8. Do you agree that the design of the system outlined in Chapter 3 achieves parity between those who will be able to access their pension flexibly and those who will be able to access their annuity flexibly? Are there any other tax rules which the Government would need to apply to individuals who had assigned their annuity income?

The system outlined in Chapter 3 appears to achieve parity between the current pension freedoms and the proposed annuity assignments. The only incongruence is not allowing all annuitants to sell their annuities as outlined in our response to question 6.

We are not aware of any other tax rules that need to be applied.

Question 10. What consumer safeguards are appropriate – is guidance sufficient or is a requirement to seek advice necessary? Should the safeguards vary depending on the value of the annuity?

The complexity of the annuity assignment decision and the potential for consumer detriment indicates that guidance alone is not an adequate safeguard. Regulated financial advice may be necessary for some people.

As consumer behaviour is emerging from the new pension reforms, various issues are being brought to light such as individuals being resentful for having to pay for the cost of advice when they do not want it or that of the "insistent client" who do not want to accept the recommendation of their adviser.

The other issue is the cost of advice, especially for those with smaller annuity incomes. All of these issues could be addressed with more cost effective advice models (e.g. telephone and on line services) rather than discounting financial advice altogether.

The safeguards should only vary depending on the value of the annuity in relation to regulated financial advice. If guidance is the only safeguard, then the value of the annuity should be irrelevant.

There are two potential ways to vary the regulated financial advice safeguard: either by the value of the annuity income or the total income being received by the individual. If the safeguard is benchmarked only against the value of an annuity then the potential detriment may be increased for those on lower incomes where an annuity forms a significant part of their total retirement income. If an individual needs to prove their total income and which part of their income is comprised of an annuity, then the percentage of total income may be a safeguard benchmark. This does create complexity for the consumer and the system so making everybody seek financial advice may prove to be an easier safeguard to implement.

Question 11. What is the best way to implement these safeguards? Should the safeguards include expansion of the remit of Pension Wise?

The responsibility of implementation of the safeguards should fall to the FCA.

The current remit of Pension Wise is to outline an individual's retirement options for their pension pot. This does not include taking into account specific personal circumstances to tailor the options that'll be most relevant.

Currently, Pension Wise does not include detailed guidance on the impact of decisions on means-tested benefits or paying off debt. The annuity assignment decision falls into a level of complexity and consumer detriment that the Pension Wise service in its current format could not deal with.

These type of issues need to be handled by qualified guidance specialists. There is a current disparity between the qualifications held by Pension Wise guides hired by TPAS for telephony and those hired by Citizen's Advice to provide face to face sessions. The potential varying levels of expertise across the service make it difficult to conceive that Pension Wise is currently capable of carrying the responsibility of annuity assignment in a robust and consistent manner across all channels. It is necessary to evaluate the Pension Wise service before making the decision to expand the remit.

Question 12. Should the costs of any advice or guidance be borne by the annuity holder (mirroring the arrangements for conversion from a defined benefit scheme)? If not, what arrangements are appropriate?

If the safeguard is only extended to guidance delivered by the Pension Wise service, the session should be free mirroring the current Pension Wise delivery model. To implement any other structure would go against the principle of guidance that was announced by the Chancellor in March 2014.

If regulated financial advice is the safeguard, then the cost will need to be borne by the annuity holder. There needs to be continued work to develop the consumer understanding of the value of financial advice and the potential costs. It is a valuable service that consumers need to understand the benefit and consumer protection that accompany this type of advice.

Question 13. Do you agree that the government should introduce a requirement on individuals to obtain a number of quotes? How else should the government best promote effective competition to ensure consumers obtain a competitive price?

If the government introduces a requirement to obtain a number of quotes, this will not ensure a competitive market. Currently, it is difficult for an individual to compare annuity quotes from different providers as each provider will ask their own underwriting questions which results in a labour intensive journey to obtain multiple quotes.

To make a smoother customer journey and to ensure quotes are easily comparable, an independent and impartial comparison tool may be a solution. Using a service like our Money Advice Service annuity comparison table tool, but to generate a quote of sum payable depending on the current income, annuity features, health, etc. is an impartial way to ensure a series of quotes from different providers. As with our current tool, the whole of market should be represented so consumers can compare across the market from an independent and unbiased source. A new tool could also be extended to take the customer to the point of transaction either with or without advice should this service be required.

The use of an impartial tool should be part of the regulation issued by the FCA.

14. Does the government's approach sufficiently protect the rights of dependants upon assignment? If not, what further steps should the government take?

There should not be special consideration for different types of beneficiaries when assigning annuity rights. This creates a confusing set of rules and another barrier for consumers to participate in the secondary annuity market.

If the annuitant has a joint life annuity, it is the property of both parties and therefore both must agree to the annuity assignment before the transaction takes place. Regulation should stipulate that both parties need to agree and sign off on the assignment. There is no need to issue additional guidance to providers.

If the annuitant has purchased a guaranteed period feature as part of the annuity, the beneficiary may be a dependent, spouse or other individual. These parties may not be able to agree to the sale. Depending on the remaining guarantee period, it may not be an issue for the assignment. For example, if there are only two remaining years on a 10 year guarantee period, it may not be an issue for assignment. Further analysis needs to be done on the size of the market for this feature to understand if dependents will be impacted by an assignment.

Question 15. Should the government permit the principal annuity holder's income to be assigned while dependants retain their own income stream? Should the decision on whether to do so be left to the discretion of the parties to the transaction?

It would be more difficult to obtain quotes if the two income streams are split. While the feature maybe useful in situations of separation or divorce, it creates an additional barrier to selling that may leave the annuitant and indeed the dependent worse off than keeping the asset in the first instance.

The complexity of undertaking such a feature without regulated financial advice and potentially legal advice seems highly complex and may lead to expensive transaction costs designated by the buyer. It is inconceivable that the buyer will conduct a complex purchase without adding additional fees. If both parties do not agree to the sale of the annuity in its entirety then the assignment should not take place.

Question 16. How can the proposed consumer protections for the assignment of annuities ensure that any impact on means-tested entitlement is understood by those deciding whether to assign their annuity income?

To ensure that the impact of the annuity assignment on means-tested benefits is understood, the FCA need to provide guidelines on organisations that can help these type of annuitants. On line and printed information can provide general information but needs to be supported by telephone or face to face that can give personal advice. Each case may be different depending on a range of circumstances. As these individuals are the most vulnerable, the cost of regulated financial advice is prohibitive. Benefits agencies need to be properly trained in guidance to serve this segment. As another alternative, a voucher for free regulated financial advice could be issued to cover the cost of the appointment.

Question 17. Should those on means-tested benefits be able to assign their annuity income?

The restriction of people on means-tested benefits not being able to assign their annuities seems discriminatory. If pension freedoms are the right of all people over the age of 55 then the right of annuity assignment should be extended to all annuitants.

It is essential that all of the information and implications of annuity assignment be understood by the annuity holder before an assignment is carried out.

Currently, the Pension Wise service does not cover means-tested benefits and the potential impact on any of the current pension freedoms. Until this aspect of the service is implemented, guidance could not be offered to those on means-tested benefits wanting to assign their annuity.

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