TPAS response to 2nd hand annuity consultation

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

Since March 2014, TPAS has received many enquiries from people interested in surrendering their annuities so there is an appetite amongst customers for these reforms. Some people believe the option to cash in your annuity is already available and some people have complained that it is unfair that they cannot benefit from the new flexibilities.

The customers that have contacted us to express an interest in this option include:

- **Customers who have small annuities that make little difference to their overall income and would prefer a cash sum (a common case that we hear is customers that had to buy annuities with small AVC pots)**
- **Customers who inherently do not like the concept of annuities**
- **Customers who bought the wrong annuities for their circumstances**
- **Customer who had to buy an annuity but had no need for the income (examples are customer that have significant DB pensions but were required to buy an annuity with other pension pots)**

Annuities sold in the future may have more options and benefits so providing this option could enable some people to sell their existing annuity in favour of buying a new annuity. Many of customers express a dislike for being "locked in" to a product for life and the next generation of annuities may remove this aspect resulting in customers seeing buying an annuity as a more attractive option.

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?

The market must be competitive one, which suggests that it will be necessary for it to be open to a reasonably wide range of entities. The downside of a wide range of entities is the increased complexity for customers of choosing the buyers to approach. We know from our helpline that customers find it difficult to shop around for financial products, which was a problem with the first hand annuity market. The other downside of a wide range of corporate entities is an increased chance of scams and unscrupulous organisations entering the market and the risk of poor sales process by some of the entities e.g. initially quoting a high cash sum but final offer being significantly lower. The Government should therefore consider this question in conjunction with the structure of the market and the level of consumer protection.

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?

The customers' perception is that the 'buy back' option will be available. However, based on customers' difficulties in shopping around, the concern with the 'buy back' option is that it may result in customers defaulting into this option resulting in the risk that the customer misses out on potentially better deals elsewhere when they choose to sell the annuity. Having probably not shopped around initially, they would therefore potentially lose out financially on two occasions. It may also open up the opportunity for annuity providers to pro-actively approach customers with unprofitable annuities and entice them to sell. The Government should consider the rules for the market that could protect the customers from these risks. The proposal of bureaux and for "buy backs" to go through the bureaux too would remove this risk but may add unnecessary costs.

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?

There is a potential cost that the industry and the buyers of annuities could incur in recouping over-paid income. This may add to the costs of the entity and the industry in general. This could be to the detriment of the customer as this will be factored into the price. Any method of automating death notifications should be considered and the Government may be able to help in this area. Requiring the annuity holder to instruct the executor of their estate to notify the annuity provider would be an unfair burden on the executor, who may be unaware of the policy's existence.

5. Do you agree with the proposed approach of the Government working with the FCA regarding the fees and charges imposed by annuity providers?
It is important that any explicit charges associated with the second hand annuity market are made clear to customers as these may be significant and possibly payable even if the transaction is not completed (for example the costs of initial medical underwriting). Many customers, particularly elderly customers, may be attracted by a lump sum in exchange for their annuity payments without realising there are additional charges to pay. Therefore it is important to be transparent regarding the charges being made, both in terms of amount but also in terms of what they relate to. The consumer protection and guidance should explain to the customer how to assess the lump sum offered less any charges that may be deducted from it.

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?
TPAS has received a number of queries from members of DB pension schemes who believe that they will be able to sell their pension income in future. Therefore, if these customers are out of scope for this new market, the reasons should be clearly explained. As with "buy backs", there is a risk that some sponsoring employers may be overly keen to push the "sale" of pensions in payment to reduce the risks of running DB pensions, to the potential detriment of these customers. We know from our experience on the helpline on incentivised transfer value exercises that customers struggled to know how to assess whether these "special offers" represented a good deal, and sometimes felt under pressure to accept within a deadline, even when financial advice was offered.

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

Our experience on the helpline to date is that customers do not necessarily distinguish the source of their pension income. When this market is launched, there will be a high incidence of customers who think that they are eligible but are not. This could lead to customer dissatisfaction. In order to reduce the number of ineligible pensioners, the reforms could be extended to those occupational pensions which have been bought out in full with an insurance company (buy in or buy out basis) but whose policies might still be held in the name of the Trustees.

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 customers who had assigned their annuity income?

The proposed tax approach appears consistent with other taxation treatments introduced within the pension freedoms.

9. How should the government strike an appropriate balance between countering tax avoidance and allowing a market to develop?

There is a risk of pension scammers exploiting the market and vulnerable customers so a strong stance on tax avoidance, together with clear publicity of the risks is an important part of the overall roll out of these reforms. TPAS hears from a number of customers who have been approached by (and in some cases have transacted with) scammers and there is a concern that this market will open up new opportunities for such organisations unless proper safeguards are put in place (see response to 10).

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?

Consumer protections are critical for this market. The customer considering this option may be elderly with limited opportunity for generating income in future. The paradox is that one of the main groups of customers who might be attracted to this reform are those on very small pensions that, by their nature, will result in small cash sum payments. Hence, the requirement to get financial advice would represent a significant proportion of the total proceeds, and the payout will already have been reduced by the fixed costs of the annuity purchasers. The requirement to obtain advice, either imposed by regulation or by the provider, is causing a dysfunction in the market currently with advisers not being prepared to take on these customers or the customers not being prepared to pay a fee. This is causing customer dissatisfaction, which is being exacerbated by the rules not being applied consistently.

Choosing a monetary limit for when it is regulated that advice is required is also arbitrary and does not necessarily protect the customers who need protection and vice versa does not allow the freedom promised for other customers.

The safeguard should be that guidance, from an independent organisation such as TPAS, should be compulsory. On a voluntary basis from a regulatory perspective (although may be compulsory in the terms set out by the buyer), all customers should have access to a guidance conversation which could help to ensure that "insistent" customers, had received the various risk warnings which could follow a standard script which would need to be adhered to s. (TPAS also recommends that the current requirements for the Freedom & Choice legislation are on the same basis for DB and safeguarded benefits.)

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

The safeguards should be delivered by an independent and impartial organisation that has a high level of pension expertise and experience to deliver the guidance. TPAS is ideally placed to provide this public service. The current Pension Wise service is very specific to certain retirement options and therefore not suitable to provide this guidance within the terms of the current Pension Wise remit. If the remit of Pension Wise is extended to cover guidance for this specific area, it is necessary that the guiders have sufficient expertise to deal with this area. It will also need to be fully supported to deal with cases that may not be eligible. The service will need to cope with a surge in the first few months following launch followed by a stabilisation of demand at a lower level.

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?
Building on the response to question 10, the cost of the guidance would be met by a levy. Where a customer chooses to take regulated advice, he/she will be required to pay for it.

13. Do you agree that the Government should introduce a requirement on customers to obtain a number of quotes? How else should the government best promote effective competition to ensure customers obtain a competitive price?
The proposals that are being discussed for the secondary market for annuities would be through a broker/bureau model with no direct market. This does add a layer of consumer protection. However, the issues with this model that need to be considered are:

- **What extra cost does it add, if any**
- **Should 'Buy back' be available directly or only be through the broker model too**
- **this model is a long way from the current customer expectation that TPAS has heard on our helpline and hence communication will be important otherwise customers will think badly of the pension industry/Government which could lead to adverse press comment**

- **will this model make it more expensive i.e. lower purchase prices and complexities so the protections would actually be working against the customer**
- **multiple bureaux may result in issues similar to those with comparison websites and in consumers having to decide which one to use.**

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

- Should the government or FCA issue guidance to annuity providers about protection for dependants?
- Are there particular classes of beneficiary which require special consideration, for example minors or following a divorce or dissolution of a civil partnership?
- Are there specific equality impacts that should be considered in this context?

The Government does need to consider how to protect dependants as many will have no other sources of income upon the death of the main annuitant. There are multiple scenarios that need to be considered such as annuities with dependant pensions and court orders that specify rights to income for the ex-spouse.

As a minimum, purchasers of the annuities should be asked whether all their dependants (not just beneficiaries of the annuity contract) are aware of the implications of a sale. Consideration should be given to put in a requirement for the seller of the annuity to declare his/her dependants and those dependants are notified by the purchaser prior to pay out. This issue would also be addressed in some detail at a guidance session but this will only protect customers where the lack of recognition of the impact on dependants is unintentional.

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?

This proposal will add to complexity and costs, which in turn might reduce the amounts available on sale. There has been no indication on our helpline that customers are seeking this option. It is imperative that customers are able to assess the cash sum offered and this would be difficult to do and could lead to misunderstanding by the customer in comparing different offers. The guidance should highlight to the customer that the where the dependant still needs an income stream, selling the annuity should be questioned or the proceeds are used to replace this income.

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?

This is a topic which could be covered in a guidance session. This is also one of the "sense check" questions which a provider could be asked to raise with the potential seller for any sale.

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

As long as those on means-tested benefits are aware of the potential impact on benefits from a sale and how the deprivation of assets rule may apply, there is no particular reason why they should not be covered by the reforms. Some pensioners on low incomes might benefit more from a lump sum payment (to pay off debts for instance), than they would a very low level of regular income.

18. What are the likely impacts of the government's proposals on groups with protected characteristics? Please provide any example

During the guidance or advice on accessing the DC pot, the guider or adviser will need to inform the customer to consider the option of converting the fund on a guaranteed annuity rate and then cash the annuity in on the second hand annuity market. Hence, this reform should increase the number of guaranteed annuity rates that are converted.