Response to proposals to create a secondary annuity market

The Money Charity is the UK's leading financial capability charity.

We believe that being on top of your money means you are more in control of your life, your finances and your debts, reducing stress and hardship. And that being on top of your money increases your wellbeing, helps you achieve your goals and live a happier more positive life as a result.

Our vision is for everyone to be on top of their money as a part of everyday life. So, we empower people across the UK to build the skills, knowledge, attitudes and behaviours, to make the most of their money throughout their lives.

We believe financially capable people are on top of and make the most of their money in five key areas:

- Planning (including budgeting)
- Saving
- Debt
- Financial services products
- Everyday money (including wages, cash, bank accounts)

The MONEY Charity

Introduction

1. We welcome the opportunity to respond to this consultation, and to provide a financial capability perspective on the proposed creation of a secondary annuity market.

2. Throughout the pension reforms already enacted, we have been extremely concerned that insufficient attention has been paid to people's ability to take the complex financial decisions that they now have to consider, at and throughout retirement. We have made this point on several occasions in response to formal consultations[1 2 3], and repeat here that without action to improve such decision-making there is a severe risk of widespread consumer detriment.

3. The introduction of Pension Wise as part of the April 2015 reforms was welcome in principle, but we are disappointed by its scope as a whole and the lack of interactivity in the online channel in particular. We recognise that the proposals in this consultation are a logical extension of freedom and choice in pensions, but these freedoms require far greater financial capability and engagement from consumers than the previous regime to avoid negative outcomes, and consumers will need greater support to not just understand their options but to apply those options to their own situation.

4. Allowing annuity-holders to assign their annuity rights to third parties will require further consumer protection measures to mitigate the risk of detriment. A consumer assigning their annuity rights will have incurred two sets of charges on the same pot of money – one when purchasing the annuity (in the form of the provider having built a profit into their model and payment levels) and one when assigning the rights (in the form of fees, charges, and a lower lump sum than the assumed value of the annuity). Therefore there is a risk that consumers could be left with a considerably lower lump sum than that with which they originally bought the annuity due to fees, charges, and profit margins.

5. Converting a guaranteed income to a finite pot that can be flexibly accessed will require a consumer to engage differently with their pension, and raises the same issues of money management and potential inadvertent exhaustion of their pension pot as we have previously highlighted. We would again urge Government to improve the support available to engage consumers with their money and help them to take decisions (which should be throughout life, not simply at retirement). Without this, consumers will be badly let down by Government, even as many of them welcome the principle of the reforms.

6. We have responded in more detail to specific questions below.

[1] http://themoneycharity.org.uk/media/The-Money-Charity-response-to-Freedom-and-Choice-in-Pensions.pdf

[2] http://themoneycharity.org.uk/media/The-Money-Charity-response-guidance-guarantee-and-pension-reform.pdf

[3] http://themoneycharity.org.uk/media/Submission-to-retirement-income-market-study.pdf

Q1: In what circumstances do you think it would be appropriate to assign one's rights to their annuity income?

7. In practice we believe there are relatively few circumstances in which a decision by an annuity-holder to assign their rights to a third party would be an appropriate one.

8. These circumstances could include the following:

    - Where an annuity-holder has developed a life-limiting condition and would find a lump sum more immediately useful than an income stream.
    - Where an annuity-holder is in urgent need of funds, for example if they are facing repossession.
    - Where an annuity-holder's current annuity income is small and does not contribute to their general financial wellbeing, but the amount they could receive by assigning their rights is more significant.
    - Where an annuity-holder is in receipt of multiple annuities and wishes to convert one or more annuities to inheritable wealth.

Q2: 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?

9. We agree that retail investors should not be able to purchase annuity income due to the complexity of the product. We do not have a view on the question of which corporate entities should or should not be permitted to purchase annuity income.

Q3: 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?

10. We see no reason to prevent annuity holders from accessing the value of their annuity through 'buy back', and believe that the risks set out in Chapter 2 are manageable.

11. The process of buy back differs from the assignment of rights to a third party as it simply consists of a provider ceasing regular payments in return for a lump sum. This should make it a simpler process, and given the reduced administrative costs, could improve value for the consumer.

12. The first risk set out in the consultation response is that annuity providers may be pressured into purchasing their own annuities, leading to potential solvency issues. However, in our view those providers who do not wish to offer buy back should be able to resist such pressure, and we do not see this as a convincing reason to prevent buy back.

13. The issue of consumer protection – and the risk that consumers do not shop around and instead default to assigning their rights to their current provider – is more pressing. The FCA's recent research into the annuity market[4] and cash savings market[5] has clearly shown the power of inertia and consumers' tendency to stick with an existing provider. We believe that this risk can be mitigated by measures discussed later in this consultation response, such as requiring customers to obtain a minimum number of quotes before assigning their rights or buying back their annuity.

Q5: Do you agree with the proposed approach of the government working with the FCA regarding the fees and charges imposed by annuity providers?

14. We agree that government and FCA should monitor fees and charges imposed by annuity providers and work together to address any issues in line with the FCA's existing powers and objectives.

15. However, given the potential for consumer detriment in this market, the FCA should be proactive in this area and work with industry before the proposed changes take effect in April 2016 to establish some 'rules of thumb', to ensure consumers who take immediate advantage of the reforms are not penalised in the form of high fees and charges.

Q6: 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?

16. We agree with the scope of this measure.

Q10: 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?

17. Ideally consumers would take advice before assigning their annuity rights, as this is a complex decision that could have significant implications for the rest of their life. However, we recognise that the cost of advice at present makes it an unviable option

[4] http://www.fca.org.uk/news/fca-finds-annuity-market-not-working-for-consumers-competition-market-study-launched

[5] https://www.fca.org.uk/news/cash-savings-market-study

for some consumers, and so we do not believe that a requirement for all annuity-holders to seek regulated advice before assigning the rights to their annuity would be appropriate. This is particularly true for consumers who wish to realise a lump sum to, for example, repay debt, who might be unable to meet the up-front cost of advice.

18. The onus should be on the industry to develop advice models than can service such consumers' needs - the development of simplified advice could lower these costs, but such a market is not yet mature enough to bear the potential weight of demand. We recognise the value of both generic and regulated advice in this context, and hope that the industry, government and the FCA will work to make simplified advice a more mainstream proposition, as well as improving the availability and operation of generic advice.

19. There is a case for requiring individuals with larger annuities to seek advice, and we suggest that this is set in line with the threshold for requiring advice on DB to DC transfers (currently at a transfer value of £30,000).

Q11: What is the best way to implement these safeguards? Should the safeguards include expansion of the remit of Pension Wise?

20. Pension Wise is already available to individuals once they have retired, and they are already able to access the service multiple times if they wish. We would absolutely expect its remit to expand to cover additional options available to retirees beyond the initial crystallisation of their pension pots.

21. However, as we state in the introduction, the Pension Wise service as currently constituted does not go far enough in helping consumers to make a decision based on their circumstances (which is distinct from giving them information about the options available to them). This is a wider question than the scope of this consultation, but it is critical to the success or otherwise of pension reform.

Additional safeguards

22. There are a number of further steps government should take to ensure consumers are sufficiently protected. These are, in our view, essential to enabling consumers to make informed decisions about assigning their annuity rights, and if they are not achievable at present this policy should not be implemented until the steps can be taken.

Ensure that historical mis-selling of annuities that have since been assigned is addressed

23. We welcome the FCA's recent action on historical annuity sales practices, and hope that this focus will continue. It is important that holders of standard annuities who assign the rights to that annuity, and are later found to have been eligible for enhanced annuities, do not relinquish their rights to compensation, and that they are also reimbursed for advice they have taken about assigning their rights.

Introduce a 'backstop' to ensure annuity-holders are aware of the Pension Wise service

24. As part of the consumer protections introduced alongside the pension freedoms from April 2015, product providers are required to ask consumers whether they have taken guidance from Pension Wise. This requirement should also apply to purchasers of existing annuity rights, especially as those who have already retired and purchased annuities might be unaware of Pension Wise (as they would have had no reason to access it).

Monitor characteristics of those assigning the rights to their annuities

25. Allowing a consumer to assign their annuity rights is another major change in the pensions landscape. Particularly in the years following the reforms, the FCA should monitor the characteristics of those consumers who do assign their rights and the characteristics of the annuities they assign. This will provide an opportunity to identify unanticipated issues of consumer protection that might arise as this market develops.

Q12: 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?

26. As we have set out previously, we feel strongly that Pensions Wise needs to be significantly improved if we are to avoid significant consumer detriment. In particular, the online offering is currently neither advice nor guidance. It offers no ability to engage with the issue by entering personal details or answering questions about risk appetite etc. This needs to be significantly improved.

27. We also believe that if the secondary annuity market becomes an option, then Pensions Wise should be extended to cover this option. Again this needs to be more than simply information but an opportunity for the individual to engage with their own personal circumstances and the risks involved.

28. The costs of the extended Pensions Wise should continue to be raised via an FCA levy on the industry.

29. We agree that for those who require (or are required) to take regulated financial advice, the cost of this should be borne by the annuity holder.

Q13: 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?

30. We agree that requiring individuals to obtain a number of quotes would help consumers to obtain a competitive price (although this will depend upon a sufficient number of market participants with an interest in purchasing annuity rights). As we suggest in Paragraph 13, this would also overcome the risk of inertia were 'buy back' permitted.

31. This would be a stronger protection than simply making consumers aware of their 'open market option', and the nature of exchanging an annuity for a lump sum makes it far easier for consumers to make decisions than if they buy an annuity with a DC pot. Differences between periodic amounts paid by different annuities can look very small, even if over time they are significant. But if a consumer assigns their rights, the quotes they will receive will be immediately-realisable lump sums, making that comparison much easier.

32. We also believe that annuity providers should be required to give the estimated remaining value of the annuity. When a provider offers an annuity, it makes an assumption as to how long the consumer will live and how much they will pay out over that period. Where a provider has agreed that the rights to the annuity can be assigned to either a third party or bought back, that provider should at a minimum tell the consumer the difference between the amount they initially assumed they would pay out and the amount actually paid out so far. This will provide an starting point against which consumers can evaluate the lump sum offered, and we expect that this would be achievable at minimal cost to providers.

33. In some cases the estimate we suggest in Paragraph 29 will still be accurate, particularly when the estimate is given relatively soon after the annuity-holder took out the policy. In other cases, for example where a consumer's life expectancy has deteriorated or improved, it will not. So we also support the proposal in Paragraph 4.17 of the consultation document to require a benchmark selling price. This benchmark price should be provided alongside an estimate of the amount the provider *now* expects to pay out in annuity income – i.e. taking into account changes

in life expectancy. This would allow the consumer to compare the amount they might receive by assigning the rights to the amount they might receive over their lifetime, and make a more informed decision.

Q15: 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?

34. If it is technically achievable, we see no reason to prevent a principal annuity holder from assigning their income while dependants retain their own income stream. For joint life annuities that have already been purchased, dependants' income should not be assigned without the written consent of all named parties. When the annuity was originally purchased there was no prospect of that annuity being cancelled or assigned to a third party, and the dependant had a very clear expectation of receiving that income upon the annuitant's death. Therefore, it would be unfair for the principal annuity holder to be able to unilaterally remove the benefit to the dependant.

35. For joint annuities that are purchased after the measures in this consultation come into effect, we believe it is reasonable for the principal annuity holder to be able to unilaterally assign the annuity rights. This is because the product would be purchased in a very different environment, where the purchaser and dependants would not expect the decision to purchase an annuity to be completely final and irreversible.

Q16: 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?

36. This is a matter for government to determine, and should form part of Pension Wise's service. As part of the Pension Wise service for consumers considering rights assignment, there should be clear information on how the assignment of annuity rights to a third party would affect means-tested benefits, and the tax implications of receiving a lump sum. This should include circumstances under which whether assigning annuity rights and spending the lump sum will classify as 'deprivation of assets' in the means test for care home provision.

Q17: Should those on means-tested benefits be able to assign their annuity income?

37. We see no reason in principle why means-tested benefit recipients should not be able to assign their annuity income. To prevent them from doing this would be inconsistent with the freedoms available to those now approaching pension age and therefore the overall thrust of this consultation.