EXTENDING PENSION FREEDOMS TO EXISTING ANNUITANTS

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The Government has launched a consultation on allowing existing annuitants to exchange their annuity for a lump sum or flexible income. The new rules won't come into effect until April 2016.

Following the Freedom and Choice in pensions reforms in the March 2014 Budget, there's been concern in the consumer media about people who consider themselves to be locked into poor value annuities. The Government responded in the March 2015 Budget by proposing further reforms from April 2016 that will enable individuals to sell their annuity without incurring a penalty tax charge. The DWP has issued a consultation to consider how best to implement the changes.

THE PROPOSALS

The Government proposes to remove the current tax charge (which is normally 55%, but can be up to 70%) for those assigning their annuity, and aims to encourage a secondary annuity market.

It proposes that annuitants will be able to sell their annuity to a commercial third party (not the current provider) in exchange for:

- a lump sum, taxed at their own marginal rate of income tax
- flexi-access drawdown (FAD) or a flexible annuity, with no immediate liability to income tax. Withdrawals will be taxed at their own marginal rate. There will be no entitlement to any tax-free cash and there will be no test against the LTA.

Any lump sums paid to the annuitant will be in their inheritance tax estate immediately. The same death benefit options will apply to FAD and flexible annuities as explained in Chris Jones' article on page 18.

The ongoing income received by the purchaser will be taxed as trading or miscellaneous income, not as pension income.

POTENTIAL BARRIERS

The consultation also covered the range of potential barriers to be overcome. There are significant consumer protection considerations, as individuals will be giving up a guaranteed income stream in exchange for a lump sum, without necessarily appreciating the longevity risk. The Government may extend the scope of the Pension Wise service, or even require compulsory regulated advice for anyone considering selling their annuity.

There's a need to take into account those other than the annuitant who are provided for under the existing annuity. For example, someone who could benefit from a dependant's provision or any guarantees.

The Government is clearly concerned that some people might sell their annuity, spend their funds and increase their reliance on means tested benefits such as Pension Credit or Housing Benefit. So a possible restriction preventing anyone receiving means tested benefits from selling their annuity is also under consideration.

CONSULTATION DETAILS

The DWP consultation 'Creating a secondary annuity market: call for evidence' is open for responses until 18 June 2015. You can find full details here:

https://www.gov.uk/government/consultations/creating-a-secondary-annuity-market-call-for-evidence