Institute and Faculty of Actuaries

Withdrawing relief for interest on loans to purchase life annuities

HM Revenue & Customs

Consultation Response

30 September 2013

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

Institute and Faculty of Actuaries

Judith Diamond
Room 3C/04
HM Revenue & Customs
100 Parliament Street
SW1A 2BQ

30 September 2013

Dear Judith,

Consultation response: Withdrawing relief for interest on loans to purchase life annuities

The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to this consultative document. This response has been prepared by the IFoA Life Assurance Consultations Committee whose members have experience of working within the Life Assurance industry.

Question 1

This relief was originally intended to allow insurers to design products that enabled property owners to take an income from their property without selling it; a type of equity release product. The continuing tax relief given on interest payments was integral to the design of these products and removing it will have a direct impact on the incomes of those individuals who took out these products and still hold them.

The products in question are a combination of a loan secured on the property and an annuity. The type of annuity used for these arrangements was a "purchase life annuity", rather than a pension annuity, and it was normal for life companies, when setting the rates for these products, to take into account their expected tax treatment. The products worked for individuals where the after tax income from the annuity was greater than the net interest on the loan used to purchase it. Removing tax relief on the loan interest payments now would increase the cost, by 20% for a basic rate tax payer, or 40% for a higher rate tax payer and it is highly likely that, in either circumstance, the annuity payments will no longer be sufficient to cover the cost of the interest payments. Rather than being a source of income for the individuals who bought these products they will now almost certainly become a source of financial strain.

The IFoA's understanding is that these contracts were normally written to last for the rest of an individual's life time and neither the loan nor the annuity would have break clauses. Thus, it is likely that such individuals will not be able to cancel or change their contracts if the tax treatment changes.

All of the individuals affected by these proposed changes will be aged 85 or over and it is quite possible that some of those individuals who will see a (possibly substantial) fall in their incomes will be at a point in their lives where there are limited opportunities to take other actions to supplement their income from elsewhere – for example, it is unlikely that many of those aged 85 and older will be able to return to the labour market. The individual consequences could be significant and might include individuals having to sell their homes, or being unable to support nursing home fees or suffering other hardship.

Question 2

As outlined in our answers to question 1 it would be critical for HMRC to understand the policy implications on products designed to make use of this relief before removing it. We would therefore recommend that HMRC surveys authorised insurers to ascertain if any of these policies do still exist before removing the relief.

Question 3

The relief has not been available to new customers for some time. As a result we don't see that there are any implications for the ongoing operation of equity release or other product markets if it is removed for existing customers.

Yours sincerely,

David Hare
President, Institute and Faculty of Actuaries