THE INSIGHT SHARING PENSIONS AND LIFETIME SAVINGS ASSOCIATION

ABI

SMALL POTS CROSS-INDUSTRY CO-ORDINATION GROUP: INITIAL UPDATE REPORT

September 2021

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FOREWORD

*By **Andy Cheseldine**, Chair of Small Pots Cross-Industry Co-ordination Group*

This Co-ordination Group is building on the work of the previous, DWP chaired, Working Group. It is primarily industry driven (and funded) because it is our problem to sort out. We have however, benefited from significant input from regulators for which we are grateful. Our purpose is twofold: to reduce the future proliferation of small DC pension pots with their detrimental effect on member value for money and to reduce the existing stock of such small pots that has already been built up.

To give some idea of the scale and context, we believe that there are:

- More than 3 million deferred savers, invested in default options, with pot sizes of under £100
- A total of 10.5 million with pot sizes under £1000, and
- If we do not do something there could be a total of 27 million pots of under £2000 by 2035[1]

There are arguments for some members maintaining some small pots – flexibility at retirement, special investment guarantees (including With Profits and those self-selecting their asset allocation), potentially more flexibility on tax treatment on pots under £10,000 (if you want to continue contributions over £4,000 per annum) and maintaining rates of protected tax free cash (but only in respect of pre-2008 funds). But these are relatively small subsets of the small pots universe and, importantly, we can ring fence and protect them with our proposed recommendations.

As you will see from the bulk of this report, we have considered:

- The current position – large numbers of micro and small DC pension pots, their numbers a negative consequence of the overall far more positive outcome of automatic pension enrolment.
- The problem – consumer detriment through duplication of charges, lost/forgotten pension pots and confusion as well as industry inefficiencies.
- Possibilities – there are a number of different potential solutions. Partly because there are a number of underlying problems we need to resolve. We believe we have considered all the relevant solutions and tried to identify the optimum answers.
- Proposition – or recommendations include what we believe, subject to the evidence currently available, and are designed to be as simple as possible under the principle of Occam's razor ["entities should not be multiplied beyond necessity", often simplified further to "the simplest solution is usually the best."].

Our proposed solutions vary – because we face a number of fundamentally different problems:

- "Stock" existing small pots and "flow" future small pots arising from new scheme leavers; the optimum solutions are different.
- Trust-based vs contract-based pension pots – the legislation (and regulators) are different and require different approaches, but it would be perverse to only try to solve one.
- "Push" (provider driven) solutions vs "pull" (member driven) consolidation – both are necessary to minimise member detriment.

1 https://www.pensionspolicyinstitute.org.uk/media/3545/20200723-deferred-members-final-report-for-the-website.pdf

We believe we have enough evidence to get started. That doesn't mean that we are completely satisfied and there are a number of areas where we are pushing for further research. But future further research is intended to let us hone our recommendations and provide the complete evidence necessary to justify any new regulatory or legislative changes.

Our key initial "considerations" for regulatory change include regulation permitting transfers without member consent (in both trust and contract based environments) where providers can show it is in member interests and further discussions about regulatory and trustee acceptance that an increase in member borne charges (within the charge cap) does not necessarily indicate a reduction in value for money for very small pots.

Further considerations are likely to emerge as our work progresses.

There is general acceptance that industry may only be able to go so far without regulatory intervention, but it is important that we start the process and clearly articulate what changes are needed. This is our opportunity to significantly improve value for members and to implement an enhancement to the foundations of automatic enrolment for generations to come.

I would like to thank all those at the PLSA and ABI who have supported us throughout our deliberations, especially those who have put pen to paper in producing this report.

Also to all those involved in the Co-ordination Group (see Annex 2), particularly those chairing the various Working Groups – your hard work is enormously appreciated. Thanks also to the representatives of DWP, TPR and the FCA who have input and critiqued along the way to help us make practical recommendations. And last, but by no means least, a thank you to the Minister for Pensions and Financial Inclusion, Guy Opperman, who has supported us throughout.

EXECUTIVE SUMMARY

Small Pots Challenge

- Automatic enrolment has been very successful in getting millions more workers to save for later life. However, making workplace pension saving the norm, including for lower income earners and people who move jobs frequently, has created a higher risk that, without active engagement, many individuals' pension savings will become fragmented in a number of deferred small pension pots in the automatic enrolment workplace pensions market.
- Last year, the PPI estimated that the number of deferred DC pension pots in Master Trust schemes alone is already approximately eight million, with the ratio between active and deferred pots reaching 50:50 in April 2020, and the number of small pots potentially increasing to 27 million by 2035 if no action is taken [2]. Left unchecked, small inactive pots risk undermining the financial sustainability of the automatic enrolment market.
- Savers stand to benefit from the consolidation of deferred small pots, if solved in the right way, through reduced complexity and greater efficiency in the pensions system when the number can be meaningfully reduced. In many cases, this should benefit all members (not just those with deferred small pots) through lower costs and charges and/or an improved member services and experience.
- The ambition of this work is to replicate the success of the automatic enrolment default model by introducing a process by which small pots are automatically consolidated within automatic enrolment workplace schemes, but which also enables members to opt out. This can only work if the cost of the consolidation process can be minimised, so that efficiencies realised can be passed on to savers, and if the potential detriment to any individual saver can be kept to levels that would be considered fair and reasonable. Until a low-cost, at scale transfer system is available, a legislative solution implementing a mass scale consolidation system will not be possible.
- Any automatic solution also needs to retain members' ability to consolidate pots proactively if they so wish.
- Similarly, the cost of any longer-term solution should be balanced against the current cost of administering deferred small pots. A solution should result in efficiencies when compared with the status quo, but meaningful success is only possible if it can operate at a low-cost and prevent further erosion of value in small pots. A wider consolidation solution therefore needs to prioritise the balance of cost and benefits to savers, while also strengthening the financial sustainability of the automatic enrolment market. These points will be key to address in a cost/benefit analysis.

Small Pots Cross-Industry Co-ordination Group

- The Small Pots Cross-Industry Co-ordination Group was jointly convened by the PLSA and ABI to make progress on operational and administrative challenges, which will be necessary to overcome for a mass transfer and pot consolidation system to be implemented. The Group was set up following a DWP Chaired Small Pensions Pots Working Group which was established in 2020. Three sub-groups of the Co-ordination Group were formed which focus on Transfers, Data Standards and Consumer Detriment and are comprised of volunteers representing different elements of the industry.

2 https://www.pensionspolicyinstitute.org.uk/media/3545/20200723-deferred-members-final-report-for-the-website.pdf

- This report captures the conversations that have been held at the Working Groups so far and highlight where broad agreement has been reached, evidential needs identified and what further steps need to be addressed to make progress to the next stage of this work.

Summary of progress

- The Co-ordination Group has progressed work on administrative issues associated with small pots and small pots solutions by agreeing a list of working assumptions. These include, but are not limited to, the potential future models under consideration, the nature and value of small pots assumed to be the starting point within scope of any future small pot consolidation model.
- Pot sizes, governance structures, fees, charges and value for money have all been identified as key areas where further analysis is needed.
- The Consumer Detriment working group has considered the potential benefits and detriments of consolidating small, deferred pots for savers and in the next stage of the work these benefits will need to be quantified.
- The Transfers working group have mapped the current individual member-initiated transfer process to identify where costs occur and discover potential efficiencies. Key barriers for low-cost transfers have been identified including those that are legislative and regulatory, and recommendations made to reduce these.
- The Data Standards working group have identified data availability and quality as key issues in data matching for small pots and the importance of these factors in making progress on administrative issues should not be underestimated.
- The Co-ordination Group has identified and analysed common elements between the future potential small pots solutions (in so far as they are currently understood) and other ongoing industry work and illuminated the opportunities and barriers for reuse.

- This Group is part of a longer-term process looking towards an eventual automatic solution that works across both trust and contract-based automatic enrolment workplace pension schemes.
- In the next phase of the work, the Co-ordination Group will consider some of the questions that have arisen through the lens of the different consolidation models set out by the DWP Chaired working group report.

Summary of initial Co-ordination Group conclusions

We believe that the following are likely to benefit savers with small pots:

Administrative issues

- Further understanding of the reliability of matches using existing data criteria and understanding how far a unique identifier can overcome some of the inefficiencies with existing data.
- Providers will work with employers and government to improve data quality, where they are able to, for example, government could help to verify data held by schemes. Particular focus should be placed on the need to provide sufficient data for effective member matching as part of employee set up.
- Update regulatory guidance to require trustees or scheme providers to keep personal contact details (including email) as already prescribed in the legislation. Expanding common data requirements to include holding saver mobile phone numbers might also be helpful.
- Consideration of the feasibility of a low-cost, at-scale transfer process for small pot consolidation initially between master trusts, and potentially with wider application.
- Consideration of other studies or pilots to consider the feasibility of a low-cost at-scale transfer process for small pots as appropriate.
- Co-ordination between the Small Pots Co-ordination Group and the Pensions Dashboards programme to explore opportunities and challenges of closer alignment; particularly learnings from data matching and data standards.
- Small pots data matching protocols align with those for Pensions Dashboards and should be considered as part of the ongoing work by PASA, PLSA and ABI on Pensions Dashboards Data Matching Conventions (DMCs), whilst recognising that the different context of small pots consolidation may require stricter criteria.
- Ensure that the current phase of industry development supporting Pensions Dashboards, such as the design and build of ISP services, is informed and aware of the future matching requirements of Small Pots.
- We recommend focusing resources on getting the Pensions Dashboards core eco-system set up and running, rather than diverting attention to Small Pots requirements, but with the caveat that the successful vendor should be kept abreast of developments on Small Pots so that this can be taken account of in decision making, but without delaying the pensions dashboards ecosystem development timeframes. Additionally, other vendors may be more suited to delivering a small pots solutions.

Factors of assessment of future consolidation models

- Identifying preferred consolidation model(s) and key elements of the legislative and regulatory framework.
- Further consideration of the conditions for transferring small pots under an automatic small pots solution and the balance of potential detriment and benefits to savers, and delivering a low-cost process.
- Review and agree assumptions for a small pots ecosystem and develop high-level process maps for both “push” and “pull” models.
- Once further model design work is undertaken, the pots in scope should be modelled against them to assess the impact on savers and the automatic enrolment market.
- Request for TPR guidance to support transfers between charge capped default funds within authorised master trusts.

Implementation of future consolidation models

- Pots within scope of future automatic transfers should be:
  - Small deferred pots within default funds and Sharia funds under qualifying schemes.
  - A suitable trigger for identifying a deferred pot and when it can be transferred need to be considered against the different consolidation models and as part of the consumer journey research and labour market analysis.
- Agreed definition of a deferred small pot member within legislation.
- Automatic transfer opt-out embedded in existing customer communications e.g. new scheme documents.
- Exemptions for small pots automatic transfer process from existing requirements, i.e. COBS 13.1 and SMPI (Disclosure Regs 2013).
- Consideration of small pots carve out or other solutions in upcoming regulatory initiatives.
- Encouraging digital communication, making sure pension communications can be effectively sent and received by email and SMS i.e. by including personal email as a required item within automatic enrolment jobholder information.
- Implementation of a small pots solution should be staged, starting with what is possible within the current confines of existing legislation.

Adjustments to these conclusions and additional conclusions are expected and will be included in the next report of the Co-ordination Group which will reflect all the work undertaken in 2021.

INTRODUCTION

BACKGROUND TO THE CO-ORDINATION GROUP

The Co-ordination Group was jointly convened by the PLSA and ABI to make progress on operational and administrative challenges, which will be necessary to overcome for a mass transfer and pot consolidation system to be implemented to address the small pots problem. Three sub-groups of the Co-ordination Group were formed which focus on Transfers, Data Standards and Consumer Detriment and are comprised of volunteers representing different elements of the industry.

The Co-ordination Group was set up following a DWP Chaired Small Pensions Pots Working Group, which reported in December 2020.

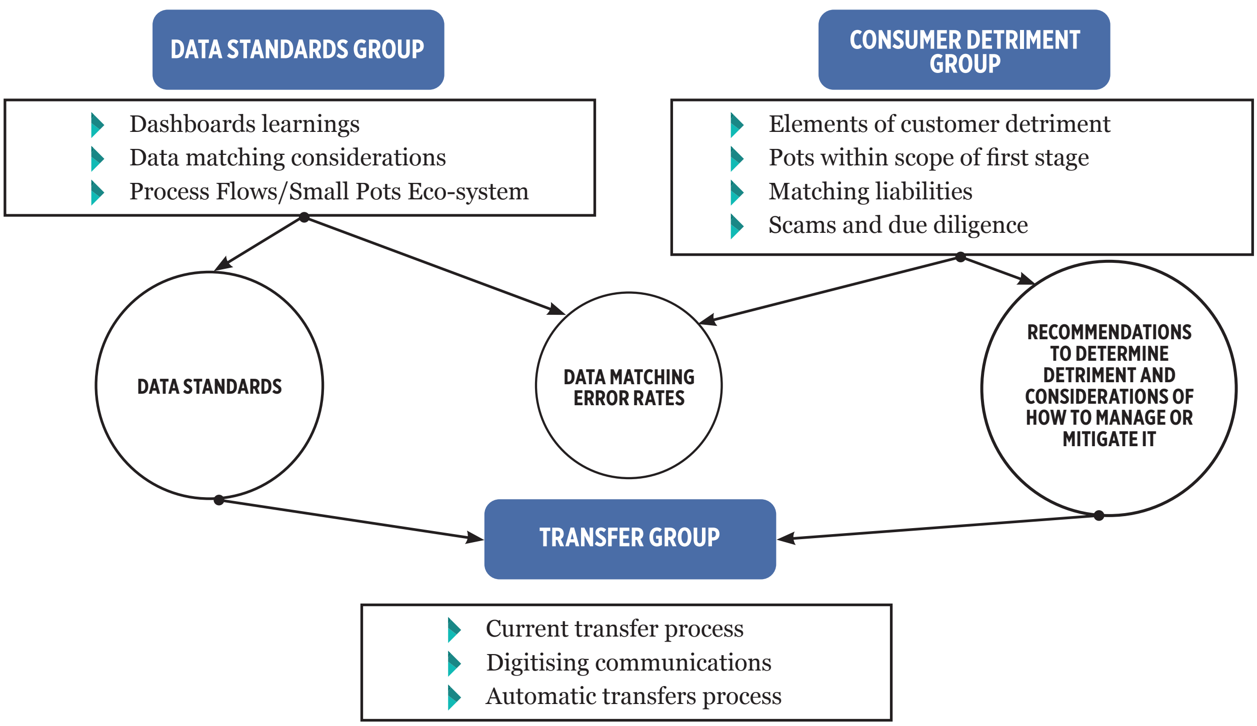
Over the first part of 2021 the Group and Working Groups have looked at identifying the barriers to delivering any solution to the small pots problem and the issues that would need to be addressed, by considering:

- potential consumer detriment and opportunities to maximise positive outcomes,
- data-matching requirements and common data standards,
- deferred small pots and schemes in scope, and
- requirements for a low-cost transfer process.

The Group has also been monitoring other industry initiatives which are seeking to address the small pots problem within the automatic enrolment workplace pension market, including the Member Exchange pilot which is currently being undertaken by a sub-group of authorised master trusts.

The outcome of these discussions and initial conclusions on these topics are covered in this report.

Connections between the working groups



THE SMALL POTS PROBLEM IS A RESULT OF THE SUCCESS OF AUTOMATIC ENROLMENT

Automatic enrolment has successfully extended pension saving to millions of today's workers. In 2020, 88% of eligible employees were enrolled in a workplace pension scheme compared to 55% in 2012 before the implementation of automatic enrolment [3]. This means over 10 million more people are now saving into a workplace pension [4]. Employers, pension scheme providers, trustees and private sector delivery partners throughout the supply chain have been central to this success.

However, making workplace pension saving the norm, including for lower income earners and people who move jobs frequently, has created a higher risk that, without active engagement, many individuals' pension savings will become fragmented in a number of small pension pots. Frequent job moves throughout a saver's working lifetime may mean an individual does not have time to build up larger pots and so have multiple pots spread between a number of different providers and schemes. Deferred small pots may also be created when savers opt out after a short period of saving or if their eligibility to be automatically enrolled is corrected or changed (i.e. if they have inconsistent incomes which means they fluctuate above and below the automatic enrolment earnings trigger). More evidence is needed to fully understand the drivers of small pot creation and their relevant impact. Although, small pots seem to be by-products of the dynamic UK labour market and the way that automatic enrolment in the UK operates, for example, the 2020 Working Group report analysis suggested that around two-thirds resulted from moving jobs[5]. There is also a fundamental evidence gap on the scale and nature and distribution of small pots in the automatic enrolment market – which may influence decisions on solutions.

The Small Pots challenge was examined in the 2020 Small Pots Working Group report [6]. This identified that the number of deferred, DC pension pots has grown substantially since the introduction of automatic enrolment in 2012. Government modelling conducted in 2012 estimated that automatic enrolment was expected to create around 50 million deferred pension pots by 2050, around 12 million of which would be under £2,000 and 33 million under £10,000 [7]. Last year, the PPI estimated that the number of deferred DC pension pots in Master Trust schemes alone is already approximately eight million, with the ratio between active and deferred pots reaching 50:50 in April 2020, and the number of small pots could increase to 27 million by 2035 if no action is taken [8]. Left unchecked, small inactive pots risk undermining the financial sustainability of the automatic enrolment market.

THE POSITIVE IMPACT OF FINDING A SMALL POTS SOLUTION FOR SAVERS

Consolidation of small pots should result in significant efficiency gains and result in a more robust system. In many cases, this should benefit all members (not just those with small pots) through a market that provides better value for money with lower costs and charges and/or an improved member services and experience. As identified during the 2020 Small Pots Working Group, a low-cost solution is needed as otherwise the scale of consolidation required to secure these benefits will not be achieved. Until a low-cost, at scale transfer system is available, there is no legislative solution for mass scale transfers / consolidation. The cost of a small pots solution needs to be balanced against the potential gains and cost savings associated with consolidating these pots.

Generally, savers will benefit from the consolidation of small pots. Consolidation will reduce the risk of pots being eroded by flat rate fees, reduce complexity and make it easier for savers to keep track of their pensions. This should encourage and support greater engagement and awareness of savings.

3 Workplace pension participation and savings trends: 2009 to 2020 - GOV.UK (www.gov.uk)

4 https://www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/automatic-enrolment-commentary-analysis-2019.ashx

5 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

6 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

7 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/191697/automatic-transfers-consolidating-pension-savings.pdf

8 https://www.pensionspolicyinstitute.org.uk/media/3545/20200723-deferred-members-final-report-for-the-website.pdf

THE NEGATIVE IMPACT OF SMALL POTS ON SAVERS

The growth of deferred small pension pots presents significant challenges, in particular for savers and pension providers as they create inefficiencies in the system and can result in poor value for members. Having many deferred small pots is not in most savers' interests. The main issues include:

- **The erosion of the pots due to cost and charges** (the recently proposed de minimis will offer some protection against this but only for pots of £100 or below). Analysis conducted by the PPI demonstrates how (without this protection) a £100 pot, deferred at age 22, with an annual flat-fee charge of £20 and an AMC of 0.25% would be eroded to zero well before the member reaches State Pension age (age 66-68)[9].
- **The inefficiency of multiple pot administration costs and levy charges** mean that the absolute level of charges borne by savers is higher than in a more efficient model.
- **Losing track of pensions and losing out on retirement income**. PPI estimated in 2018, that there were around 800,000 stranded pension pots, or an estimated £20bn in stranded savings across the UK, where providers had lost contact with the scheme member[10].
- **Confusion or perception of complexity of receiving communications from numerous schemes and sub-optimal decumulation decisions**. The 2020 Small Pots Working Group report highlighted feedback from the industry that small deferred pots could be a disincentive to member engagement due to the increased hassle and complexity of keeping track of and accessing multiple pots [11].

Small pots are also a problem for providers as administering and managing a large number of deferred small pots comes with a cost. These costs must ultimately be borne by savers (and employers) and, in the worst-case scenario, they could jeopardise the long-term sustainability of some auto-enrolment providers.

Another indirect detriment is the reduced competition in the high turnover employment sectors that may be commercially unattractive for commercial pension providers due to the likelihood that these employers bring with them a lot of small pots; these employers, and the pension scheme members, may not therefore have access to a wide range of schemes. Over time pension providers would become less efficient and, theoretically, less profitable, which could result in less available capital to spend on innovation – potentially leading to savers' service and experience suffering (such as by receiving less engaging, cheaper, communications).

STOCK AND FLOW OF SMALL POTS

A solution to small pots needs to address both the "stock" and "flow" of small pots. The "stock" of small pots can be defined as the small deferred pots that are currently in the system and being held by providers. The "flow" can be defined as those small deferred pots currently being created, and yet to be created in the future. The cause of these small pots' creation may differ and therefore, a combination of different solutions may be needed to resolve all issues associated with current and future small pots.

9 https://www.pensionspolicyinstitute.org.uk/media/3545/20200723-deferred-members-final-report-for-the-website.pdf

10 https://www.pensionspolicyinstitute.org.uk/media/2855/201810-bn110-lost-pensions-final.pdf

11 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

DWP CHAIRED SMALL PENSIONS POTS WORKING GROUP, 2020

GUIDING PRINCIPLES FROM DWP CHAIRED SMALL POTS WORKING GROUP REPORT

The 2020 Small Pots Working Group agreed on guiding principles and working assumptions which any potential policy solution would be assessed against. The Principles were:

- Build on the success and behavioural insights of automatic enrolment, and optimise retirement outcomes
- Promote value and transparency for savers;
- Minimise administrative burdens for pension providers and employers (including SMEs);
- Support competition and a vibrant pensions market for members;
- Fit with the direction of HMG's existing pension policies and reforms, including Pensions Dashboards; and
- Maximise affordability and sustainability for members, employers, pension providers and tax-payers.

The Working Group provided the Minister with a report[12] in December 2020, which included recommendations and an indicative roadmap of actions for industry, delivery partners and Government. The report included some key recommendations for the pensions industry, which are summarised below:

a. Pension providers that hold multiple pots within charge-capped default funds for the same deferred members should consolidate those pots over the next 3-4 years. However, the report recognised some of the limitations and suggested that as an interim step providers should work towards implementing a 'single member view' by 2021/22.

b. The pensions industry should establish an operational focussed group to address the administrative challenges which it will be necessary to overcome for a mass transfer and consolidation system to be implemented. This work should look at matching capability, the adoption of common data standards across industry and identify requirements for automatic and automated large-scale low-cost transfers. An update report should be published in summer 2021.

c. Progress should be made with a member-exchange proof of concept trial, involving low value small pots within master trust schemes.

d. A feasibility report on low-cost transfers should be published in Autumn 2021. Learnings from this can help to inform the administrative processes work.

e. Consolidation systems will be prioritised once operational barriers (b and c above) are reduced, but more investigation and examination of administration processes is needed. The group prioritised two models – the 'default consolidator' and automatic pot follows member.

The full recommendations on next steps for the industry and DWP are reflected in the updated roadmap, included in Annex 1.

The report also identified that technology and tools, such as Pensions Dashboards could help savers and small pots consolidation by enabling individuals to access their pensions information online, securely and all in one place. However, it also noted that by itself Pensions Dashboards would be unlikely to reverse the trend in growth of small deferred pots or remove the totality of costs in the system. Pensions Dashboards was therefore found to be one element of a wider small pots solution.

12 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

The Co-ordination Group, and this interim report, is the industry's response to recommendation 'b' above. The progress made to date by the Co-ordination Group and other industry initiatives and is summarised in the table below.

	AREA	RESPONSIBILITY	PROGRESS	LATEST EXPECTED COMPLETION (CURRENT BEST ESTIMATE)
Evidential needs	PPI Pensions Data Project	PPI	✓ Ongoing	2022
	Labour market analysis	DWP		
	Consumer testing	Under discussion		2023
	Evidencing member benefit	Under discussion		
Consolidation models	Same scheme consolidation (in line with the small pots working group report recommendations)	Industry	✓ Ongoing	2023
	Develop inter scheme consolidation models and identify preferred model	Co-ordination Group	✓ Ongoing	
Administrative issues	Identify main barriers	Co-ordination Group	Completed	
	Outline small pots eco-system	Co-ordination Group	✓ Ongoing	2021
	Exploring low-cost transfer service	Industry	✓ Ongoing	
	Improved data quality	Industry	✓ Ongoing	
	Feasibility of a low-cost, at-scale transfer process	Sub-Group of Master Trusts	✓ Ongoing	2021
	Design of a low-cost transfer service	Industry		Dependent on outcome of the feasibility report
	Data matching	Industry (including as part of Dashboards discussions)	✓ Ongoing	2022/23
	Data Standards	Industry (including as part of Dashboards discussions)	✓ Ongoing	2023/24
Other	Member exchange proof of concept and pilot	Group of master trusts	✓ Ongoing	2022

CHAPTER 1: THE CASE FOR SMALL POTS CONSOLIDATION

SUMMARY

- Savers and providers will benefit from the overall efficiency gains possible where (automatic) small pot consolidation is introduced. However, further assessment of the impacts of different solutions are needed.
- Pot sizes, governance structures, fees, charges and value for money have all been identified as key areas where further analysis is needed.
- The Co-ordination Group has gathered evidence and analysis, and has identified further evidential needs and data simulations that will help to inform the case for small pots consolidation and progress towards assessing a solution to the small pots problem.

Both savers and providers stand to gain from small pot consolidation, including where it is automatic. The table below outlines some of the potential benefits and costs that members might face from small pot consolidation without the controls we recommend in this report.

POTENTIAL SAVER BENEFITS (I.E. OPPORTUNITY COST IF NO CONSOLIDATION)	POTENTIAL SAVER DETRIMENTS	OTHER CONSIDERATIONS
More favourable charging structure	Less favourable charging structure	Sizes of transferring and receiving pot i.e. impacts on the effects of charges e.g. de minimis and fixed fee considerations
Better value for money, including net investment returns and member service/experience	Worse value for money, including net investment returns and member service/experience	Net investment returns
Avoid hassle of locating and accessing multiple pension pots	Fund is lost due to incorrect matching	Distance to retirement
Simpler and better decision making about how to use pension wealth due to reduced complexity	Loss of guaranteed benefits such as GARs and protected pension age (although this might be less applicable to small deferred pension pots in automatic enrolment workplace pension schemes)	Future contributions
Lower charges because schemes have reduced costs (due to systemic efficiency saving)	Consolidation costs increase costs to industry and members (if low-cost transfer regime is not implemented)	Transfer types i.e. master trust to master trust, trust to contract and vice versa
Better proposition and improved member service and experience (due to reinvest of cost savings by schemes and providers)	No guarantee cost savings will be reinvested by all schemes and providers	Use of guidance services and advice
Better outcomes through better use of consolidated pots	Scams risk (depending on which model is selected)	Impact of dashboards
Larger pots are more likely to engage the saver and less likely to be used inefficiently at retirement (e.g. taken as a cash lump sum)	Members may prefer to hold small pots to allow full encashment at retirement	

In particular, it is worth reiterating that savers stand to gain from:

- a reduced risk of losing track of their small pots (and the associated likely improved decision making[13]). This is most likely if a pot moves to a saver's current active pot or to a consolidator which the saver recognises or with which they have an association, and
- the systemic savings associated with a low-cost automated small pots transfer process which could lead to lower costs and charges for savers and/or improved product offerings – it is important the potential savings for the industry and the associated benefits for savers are quantified as part of the impact analysis.

Furthermore, some savers might receive better value for money in a new scheme or product as a result of higher net investment returns and/or access to a better product proposition and member services.

The consolidation of small pots is a net systemic gain and savers should share efficiency gains to the automatic enrolment workplace pensions market system, though this is not a given. Evidence on the scale and nature of the distribution of small pots in the automatic enrolment workplace pensions market, and a cost/benefit analysis of interventions and consumer outcomes will help to inform this. Removal of these small pots should result in costs savings being passed on to members, either through reduced charges or through re-investment in schemes, leading to improved member experiences. It is important to note that this is dependent on being able to build a transfer process which is as frictionless and low-cost as possible. There is a need to significantly improve the current transfer process as a pre-cursor to moving forward and reaping the benefits of consolidation, regardless of the eventual solution. This systemic efficiency benefit is harder to quantify but should be part of any future impact analysis.

In future it will be crucial to understand the net whole of market gain of removing a large proportion of small pots from the automatic enrolment workplace pensions market, so that calibration of impact tolerances to individuals can be undertaken. This is one reason why the Group continues to agree that a wider impact analysis is needed; the quantum of this systemic gain needs to be balanced against the individuals' gains or losses[14]. Where the systemic benefit is large enough, some smaller individual detriment may be acceptable within the wider benefit to many. However, further analysis is needed to fully understand this.

There are also some potential risks for savers associated with small pot consolidation which will need to be mitigated to reduce the potential for consumer detriment. For example:

- many savers will achieve better or equivalent value for money after an automatic transfer, however some might achieve lower value for money in the receiving scheme (for example, due to lower net investment returns and/or a poorer product proposition or member experience) but this is likely to be of marginal materiality for low pot sizes and outweighed by the benefit of consolidation (see section below entitled *Fees, charges and value for money*)
- there is the scope for funds to be incorrectly matched, which could see some people lose some of their savings – although the incidences of incorrect matches would be expected to be low and, in any event, this could be addressed through the introduction of a suitable industry wide compensation regime where a saver's pot is lost as a result of an incorrect match, and (see Chapter 4)
- savers might cross a regulatory boundary and be subject to different member protections as a result, which may become more important were larger 'small pots' included within any automated transfer process and the materiality of any differences increases over the life of the pot. For example, there are situations where they would no longer benefit from the trustee(s) fiduciary duty in respect of the scheme from the start to the end of their pension journey

Any automated transfer regime will also need to address the potential for fraud or scams (see section on Pension Scams), although this risk would remote for some of the models under consideration.

Later in this section protections are discussed which could be introduced to mitigate these potential risks.

13 See, for example, FCA Financial Lives Surveys.

14 See, for example, PPI analysis which suggests that by 2035 we will reach the point of one active point having to support three deferred pots, which means that greater cross subsidies are required for schemes to break even.

POT SIZE MATTERS

> *'Whereas modelling developed at the time of automatic enrolment's introduction used larger pot values (e.g. £2,000, £10,000) to delineate the parameters of the small pots challenge, the latest evidence on pot size distributions suggests a proliferation of substantially smaller pots than those that may have initially been foreseen.'* [15]

The balance of these benefits and costs may differ depending on the size of deferred pot being transferred. However, as below (see Chapter 2) the Co-ordination Group is currently focusing on trying to resolve the small pots issue in the most proportionate way and for the very small pots currently under consideration (i.e. <£500) the most important factors are how much cost (borne by members) could be reduced overall by a consolidation process, balanced with the extent of any opportunity cost in individual circumstances were they transferred to schemes providing poorer value for money.

The Co-ordination Group is not currently suggesting that for very small pots an individual value for money requirement or analysis be a prerequisite to transfer as this could negate the efficiency gains achieved, but without further analysis it is impossible to conclude this point; further consideration will be necessary in light of the different possible models.

GOVERNANCE STRUCTURES VARY

> *'However, given the changes in the operating environment and scheme quality / governance since [risks to pot erosion, automatic transfer models] was last considered it is felt some of these risks could be mitigated, for example, by requiring set conditions / parameters to be met before a transfer is agreed.'* [16]

In the trust-based system it is currently at the discretion of trustees whether to cede and receive pots, and the Member Exchange Pilot (see Chapter 7) is partly intended to deliver evidence on trustee willingness to do this. However, it is possible that some trustees may find it difficult to agree to transfer pots in circumstances where an individual might be worse off as a result, even where they recognise the potential benefits of consolidation for the sector as a whole. If this proves to be the case it could support calls for the government to introduce a mandatory small pots transfers regime, if the cost/benefit analysis supports this. Such a regime could also address a key barrier to consolidation for contract-based schemes which arises from the fact that providers cannot make a transfer without a saver's explicit consent, even where they consider this to be in the saver's best interests. Without an overriding legal obligation on contract-based providers to transfer small deferred pots, this would prevent whole of market low-cost automatic transfers of small pots.

FEES AND CHARGES

> *'Consolidation solutions present an opportunity to make the automatic enrolment workplace pensions market more efficient and improve member outcomes. The key benefits are that consolidation could reduce member charges and provider costs as members would be paying for fewer pots and providers would avoid duplication involved in administration. In order to realise the cost/benefits of consolidation models for members, further work would be necessary to understand and limit the impact of transaction costs, in addition to the pensions industry's examination of administrative processes to enable mass transfers.'* [17]

Flat fees can pose an issue in the context of small pots. Consolidation of very small pots, as anticipated at the early stages of any new solution, may mean that pots could be transferred from a ceding scheme with no flat fee to receiving schemes with a flat fee. This could result in the pot being eroded to the de minimis threshold, proposed recently to protect small pot erosion, over time. Therefore, consideration of flat fees is necessary when designing a consolidation model.

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15 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

16 ibid

17 ibid

VALUE FOR MONEY

> *'Trustees [...] would need a common Value for Money (VFM) assessment framework in order to enable pension pot exchanges without potentially creating unacceptable risk to the member or unacceptable burden on the Trustee.'* [18]

There is currently no standardised measure of long-term value for money that might allow trustees to consistently and meaningfully compare schemes and any such 'consistent' comparison of VFM between schemes will always be subject to caveats. At time of drafting, the FCA and TPR published a discussion paper assessing value for money[19]. The paper looks to open up discussion on the development of a common framework for measuring VFM with the ultimate aim of promoting consistent assessments and enabling meaningful comparisons between schemes.

In the context of small pot consolidation, the Group has considered whether that, in order for any whole of automatic enrolment market consolidation solution to be successful, it may need to be possible for small pots to be transferred from one charge capped default fund to another regardless of the specific fee level. This relies on similar logic to automatic enrolment; where schemes meet certain minimum standards (i.e. are automatic enrolment qualifying schemes) they are deemed sufficiently appropriate for members to be automatically enrolled into and therefore those same schemes should be sufficiently appropriate for small pots to be transferred into (regardless of whether the charges under the receiving scheme are higher or lower than those under the transferring scheme).

If this is not the case it would mean that small pots could only flow one way (i.e from higher charging to lower charging schemes) which would distort the auto-enrolment market and mean that the necessary scale to solve this problem would not be achieved. In addition, simply because a saver moves from a lower charging scheme to a higher charging scheme does not automatically mean that the saver will experience a poorer outcome on the basis that they may benefit from other 'value' elements, such as higher investment returns under the receiving scheme, which more than offset the higher charges. A saver may also benefit from a better proposition and better service.

However, in order to achieve this, it is likely that legislation will be required which compels trustees and contract-based providers to transfer small deferred pots that are in scope from one charge capped default fund to another without a value assessment, if overall cost/benefit analysis supports market intervention. Contract-based providers will also need to be enabled and then receive regulatory authorisation to do this given the current constraints on transfers without consent arising under their contracts with savers.

In advance of any legislative compulsory transfer framework, it could be helpful to have assurance or a statement from the Regulator to facilitate small pots transfers. As we are exploring the opportunity for transferring and consolidating small deferred pots in the automatic enrolment market, and as currently we believe the balance of small deferred pots reside in automatic enrolment master trusts, the Member Exchange pilot (Chapter 7) will inform the extent to which transferring and consolidating small deferred pots is feasible within existing legislation and current trustee comfort. It is possible that the pilot, or other work, will identify the degree to which helpful assurance could be provided by the Pensions Regulator to deliver additional comfort for trustees and relevant parties to facilitate small deferred pot transfers.

Any such assurance from the Regulator should therefore be intended to help give some comfort to trustees in the short and medium term and could help unlock solutions that could work for 'stock' pots. The Regulator may, for example, be able to provide a statement highlighting the holistic approach trustees must take, including the benefit to members of having fewer small, deferred pots. This is notwithstanding that the statement will be unlikely to establish rights savers have in the case of transfers they are not happy with (Chapter 4) or assert which schemes offer relative value for money. Particularly, some reassurance could be provided by Regulators and Government that new scams and other legislation should not be a barrier to transfers to Master Trusts (Chapter 8). The Group will continue to consider the need for supportive contributions in the next stage of the work.

18 ibid

19 https://www.thepensionsregulator.gov.uk/en/document-library/consultations/value-for-money-discussion-paper

FURTHER ANALYSIS AND SIMULATION IS NEEDED

> *'Large scale automatic and automated consolidation solutions are necessary, but implementation will involve a journey if members are to continue to benefit from a thriving and sustainable market.'* [20]

Further assessment about the net saver and system benefit to moving small pots is needed including to take account of the practical and benefit/detriment assessment, and across different models. For example, it is important to understand the cost of implementing and maintaining a small pots solution for the automatic enrolment workplace pensions market. The cost of this solution should be less than the current process to ensure it is sustainable and gains are achieved for members. A small pots solution will only be tenable if it is low-cost, otherwise at a macro level it might negate the net benefit of consolidation. This will be key to understand in a cost/benefit analysis.

Consideration is also needed in the future as to which scheme bears the lion's share of any transition costs – which can likely be equated to the cost of communication with the saver on an ongoing basis. If transfers are made of very small pots the financial benefit to the ceding scheme (i.e. the avoidance of the cost of 40 years of administration) is far more than the benefit to the receiving scheme (the AMC levied on an additional very small sum). This assessment is necessary as there may be perverse impacts to certain sections of the market depending on model agreed (for example, if the receiving scheme could choose to 'pull' the pots in any model they may look for a higher small pot threshold than any provider who 'pushes' the pots, as the receiving scheme would save most money by transferring the smallest pot).

However, discussions so far have focused on administrative elements and have considered different options for when transfers may be able to take place. We would propose as a starting point for further consideration and simulation:

- One option for transferring could be that transfers can occur where trustees and IGCs are comfortable that savers would be moving into a scheme that offers value for money. Necessarily, this would entail some sort of value for money assessment being undertaken, which would result in additional cost to the process. This method should result in strong member protections, but as previously noted, a low-cost transfer is essential for an automatic small pots solution, which means transfers may not be able to take place on this basis and therefore efficiency gains will not be made.
- Another option is that transfers between authorised master trusts and FCA regulated GPPs operating within the charge cap are acceptable. The assumption would be that those schemes operating within the automatic enrolment framework offer enough of a protection to members to enable transfers. This would result in low-cost transfers as value for money assessments would not be needed and wider efficiency gains could be made, however, some level of individual detriment may occur. This should nonetheless be offset by the benefits of consolidation, though this may be challenging to quantify.
- Transfers between authorised master trusts within the charge cap, even if to higher charging schemes, is likely to be acceptable (though should be considered further in light of different models and based on an assessment of the projected dynamic effect of shared efficiency benefits over time). This is justified given the existence of fee protections through the charge cap, similarities in governance across master trusts and the general low level and limited variation of charges across master trusts [21], which in turn mean that the potential for harm in transfers between these should be relatively small and the net benefits of consolidation are therefore much more likely to outweigh any differential in cost. In future the same justification is plausible across and between GPPs (though issues associated with contract law must be addressed foremost before this can happen (Chapter 5).

20 ibid

21 https://www.gov.uk/government/publications/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes#member-borne-charges-within-the-cap

Flat fees can introduce a complication when considering small pot consolidation as they can erode the value of a small pot:

- DWP have intervened to propose restricting the flat fee element of combination charges used by pension providers to only above a £100 de minimis level [22]. The purpose of DWP's intervention was to minimise the harm associated with pot erosion.

There are several arguments that can be made on whether to transfer small pots around the de minimis, where a flat fee is applicable:

- One option is to say that any small pots solutions overall are limited to aggregate values greater than a certain sum (e.g. £500), or solutions cannot automatically transfer a pot from a scheme where it is not subject to a flat fee (either because the ceding scheme uses an alternative charging structure, or the pot is worth less than £100 and hence below the de minimis for flat fees to be applied) into a scheme where it would be subjected to a flat fee that would erode the transferred amount. Another alternative is restricting the solution so that a pot subject to a flat fee cannot move to a place with a higher flat fee. We note that this latter alternative, however, may be far from optimal given that this leaves some of the smallest, most uneconomic pots that could benefit the most from consolidation, unmoved.

- Another argument is that the de minimis offers sufficient protection to these pots and therefore small pots should be able to move to a scheme where a flat fee is applicable. The combined value of the new pot should also be sufficient to negate the erosion of the pot due to flat fees as a small deferred pot should hopefully be combined with a higher value or growing active pot, which will not be eroded by a flat fee.

Thought would need to be given in the future as to whether the proposed flat fee de minimis is sufficient to deliver protection against fee erosion for all individuals when measured against the net potential systemic gain across individuals automatically transferred under small pot solution models.

INITIAL CONCLUSIONS

To support these future discussions, a cost/benefit analysis is essential to understand the potential individual level of detriment and whether these can be considered tolerable. In the absence of evidence on the scale of potential net member benefit then it may be too early to say that moves to higher charging schemes are likely to be needed, or indeed acceptable because they are immaterial.

As pot sizes increase above those that the Co-ordination Group is using as a working assumption (see Chapter 2) the tolerances for member detriment may shift. For example, at higher value pots, different investment performance will have a larger impact on member outcomes. For this reason, the Co-ordination Group has noted that the risk profile of including higher value pots shifts the larger the pots that are included. Different parameters may therefore be needed were higher value pots to be part of an automatic small pots solution. It is important to understand where this 'sweet spot' level is for now and in the future, and so the Group has made recommendations on the future analysis needed. Re-examination of the interaction with charge cap and flat fees may be needed at each stage were pot sizes to increase.

CONTRACT-BASED SMALL POTS DATA COLLECTION

To understand the number of small pots in contract-based schemes, the ABI undertook a data request from eight contract-based providers (both automatic enrolment schemes and non-automatic enrolment schemes). This showed that the small pots issue is not isolated to the trust-based market, and contract-based providers hold a material number of small pots that are worth less than £50 or £100. This has led the group to agree that any automatic transfer process should be trialled with pots of £100 or less before being rolled out more widely. At this scale the risk of detriment to customers in the form of higher charges is considerably lower and errors in the transfer process could be fairly cheaply rectified.

22 https://www.gov.uk/government/consultations/permitted-charges-within-defined-contribution-pension-schemes

Number and value of deferred and active pots (as of 31 March 2021)			
	Number of deferred pots	Number of active pots	Total worth (£)
Value less than £50	212,223	45,439	£6,367,216
Value less than £100, greater than £50	209,777	50,799	£19,556,127
Value less than £500, greater than £100	1,075,558	377,598	£407,817,999
Value less than £1,000, greater than £500	775,098	336,336	£814,333,240

	Cumulative number of deferred pots	Cumulative number of active pots	Cumulative total worth (£)
Value less than £50	212,223	45,439	£6,367,216
Value less than £100	422,000	96,238	£25,923,343
Value less than £500	1,497,558	473,836	£433,741,342
Value less than £1,000	2,272,656	810,172	£1,248,074,582

NEXT STEPS AND INITIAL CONCLUSIONS

We believe that the following is likely to benefit savers with small pots:

- Further consideration of the conditions for transferring small pots under an automatic small pots solution within the automatic enrolment workplace pensions market and the balance of potential detriment and benefits to savers, and delivering a low-cost process.

FURTHER EVIDENTIAL NEEDS

Across the work further evidence will be crucial to progress in taking balanced and proportionate views and delivering final recommendations. At this stage it was not anticipated that the Group would be able to take these judgements, but progress has been made to identify further information needed to enable these in the future. Broadly speaking these needs can be split by simulations of market impact and those of highest priority. The latter particularly include those that impact on model assessment starting with those that are fundamental to the potential net efficiency benefits, such as assessments of pot creation and distribution. Without these it will be very difficult to discern between different available models. Other evidential needs are likely to follow these in terms of priority and therefore timeline.

Current needs identified are as follows:

- Literature review of evidence on benefit of small pot consolidation and new research if required to evidence the intrinsic benefits to members of pot consolidation, including engagement benefits and wider choice/better value options at retirement.
- An analysis of the "system" efficiency benefits of eliminating the cost of administering small pots, with credible assumptions about the flow of these benefits to schemes and members.
- We need to understand in more detail why small pots are created, and whether employer, member or scheme solutions are therefore best to deal with the 'flow' of future small pots. Labour market analysis should be helpful in providing further data on this.
- More detailed understanding of the distribution of existing small pots across the market both by member and provider (e.g. the degree to which non-UK nationals being automatically enrolled as a result of short periods of seasonal work result in a problem for some master trusts).
- Simulation exercises to understand cross-holdings and costs of matching and transferring pots en masse.
- Consumer testing to understand views, particularly the potential consumer journey, for each automatic transfer solution, which will be crucial to making the final decision from the automatic transfer solutions that remain on the table.
- The analytical next steps identified in the Small Pots Working Group report in December 2020, other than those covered above:
  - evaluation of costs and benefits and value for money, modelling potential impacts on individuals in different circumstances.
  - more comprehensive evidence on the average size of deferred pots and how many small pots are being generated (and how many are already transferred by members).
  - further economic/market impact analysis in relation to the default consolidator model.

FUTURE LEGISLATIVE/REGULATORY CONSIDERATIONS

In advance of any legislative compulsory transfer framework, it could be helpful to have assurance or a statement from the Regulator to facilitate small pots transfers. As we are exploring the opportunity for transferring and consolidating small deferred pots in the automatic enrolment market, and as currently we believe the balance of small deferred pots reside in automatic enrolment master trusts, the Member Exchange pilot (Chapter 7) will inform the extent to which transferring and consolidating small deferred pots is feasible within existing legislation and current trustee comfort. It is possible that the pilot, or other work, will identify the degree to which helpful assurance could be provided by the Pensions Regulator to deliver additional comfort for trustees and relevant parties to facilitate small deferred pot transfers.

Any such assurance from the Regulator should therefore be intended to help give some comfort to trustees in the short and medium term and could help unlock solutions that could work for 'stock' pots. The Regulator may, for example, be able to provide a statement highlighting the holistic approach trustees must take, including the benefit to members of having fewer small, deferred pots. This is notwithstanding that the statement will be unlikely to establish rights savers have in the case of transfers they are not happy with (Chapter 4) or assert which schemes offer relative value for money. Particularly, some reassurance could be provided by Regulators and Government that new scams and other legislation should not be a barrier to transfers to Master Trusts (Chapter 8). The Group will continue to consider the need for supportive contributions in the next stage of the work.

CHAPTER 2: SCOPE, ASSUMPTIONS AND AN ECOSYSTEM

SUMMARY

- The Co-ordination Group has progressed work on administrative issues associated with small pots and small pots solutions by agreeing a list of working assumptions. These include, but are not limited to, the potential future models under consideration, the nature and size of pots assumed as a starting point within scope of any future small pot consolidation model.
- As questions remain about the future solution models, and as the Group has focused on administrative issues regardless of the model until this point in their work, descriptive conclusions have been reached in the meantime.
- Progress on different models and the ecosystem will be assessed from the Autumn.

In order to make progress on some of the key administrative issues, the Co-ordination Group agreed several working assumptions. These are:

- The group should follow the conclusions of the DWP-Chaired Working Group and consider the merits of the following future consolidation models: pot follows member, default consolidator(s) and member exchange only
- Emerging data standards (such as those envisaged for Dashboards) are a good starting point but would need developing to enable small pots matching and consolidation
- Recommending the use of Dashboards architecture and ecosystems will be helpful, even where this must be over the longer term, assuming adaptation or additions for mass transfers are possible and that this does not impact dashboards delivery
- The initial focus of scenario testing of administrative processes and potential consumer detriment in the first phase should be on very small pots i.e. ranging between £0 and £100, £100 and £250 and £250 and £500.
- Second phase work could in the future consider small pots of a higher value, including the risks of doing so.
- Sub-groups should focus on money purchase benefit pots in accumulation held within the default funds of qualifying automatic enrolment schemes with no special characteristics (such as GARs). This, however, is based on the assumption that forthcoming evidence finds this scope would have a material positive impact on the problem overall.
- There will be some matching errors, the risk of which should be minimised (as far as possible) with a suitable compensation regime introduced to protect savers.
- Members must be given the opportunity to opt out of any auto-consolidation and will likely follow the ‘path of least resistance’ anyway.[23]
- For market-wide solutions, legislation will be needed, if cost/benefit analysis supports intervention.

23 See Chapter 5

SMALL POTS ECOSYSTEM

The DWP Chaired Working Group recommended an industry group should develop common data standards to support effective consolidation. However, progress is necessarily limited given the current availability of information and design details for a potential future small pots ecosystem and assumptions made about whether the solution applies to both 'stock' and 'flow' small pots, or just one or the other of these. Industry-wide Data Standards are not solely a collection of data items but are a set of process flows, quality standards, output standards and a governance/maintenance regime for those process flows and data standards.
In order to make progress in addressing the challenges, more detail and shared understanding is needed for any potential future small pots ecosystem where required to operationalise elements of the solution. Assumptions can begin to be made based on a 'push' or 'pull' mechanism alongside considerations of member detriment:

- **"Pull" process:** The acquiring scheme initiates the process by asking all other schemes: "Do you have any relevant small pots to be consolidated?", and, where positive matches are made, requests them to be transferred from the appropriate ceding scheme(s) (i.e. the acquiring scheme "pulls" small pots towards them/a consolidator)
- **"Push" process:** All ceding schemes say: "We have these small pots to be consolidated, who wants them?", and, where positive matches are made, the appropriate ceding scheme(s) transfer the relevant small pots to the appropriate acquiring schemes(s) / a consolidator (i.e. ceding scheme(s) "push" small pots away)

In order to make progress on detailing these processes, and a small pots eco-system, a number of components of the eco-system and working suppositions need to be agreed. Further discussion is needed to confirm these, but there a number of different components that must be resolved:

COMPONENTS OF ECO-SYSTEM	COMPONENT DEFINTION	CURRENT ASSUMPTION
Model	The consolidation model used to aggregate small pots.	At this stage, process flow and ecosystem thinking should be developed which works for both the default consolidator and the pot follows member models – as prioritised by the DWP Chaired Small Pots Working Group.
Process	Whether the model follows a "push" or "pull" process as outlined previously.	Consider a "pull" process, where acquiring schemes ask all other schemes in the community: "Do you have any small pots for consolidation?", then "pull" these pots towards either a) a consolidator or b) themselves and a"push" process, where ceding schemes send pots to another provider/consolidator.
Community	Actors who are participating in a small pots eco-system / consolidation model.	Assumption that there is a defined "allow/deny list"[24] participating in the small pots consolidation regime, which is likely to be a subset of all schemes listed in the Dashboards ecosystem's Governance Register. See Section on Pension Scams in chapter 5.

24 i.e. a set list of providers or category of provider where automatic small pot transfers will be possible without due diligence checks being necessary.

COMPONENTS OF ECO-SYSTEM	COMPONENT DEFINTION	CURRENT ASSUMPTION
Periodicity	How often a “pull” or “push” process takes place to move small pots.	This needs further discussion but could be time trigger i.e.daily, monthly, yearly or based on starting or leaving employment.
Execution	Which pots should be included as part of a small pots eco-system.	Transfers should only proceed where all the small pot criteria are met. See Chapter 3.
Reuse of existing infrastructure	What infrastructure can be reused for small pots.	The process flows and ecosystem should reuse/adapt existing infrastructure where possible.

NEXT STEPS AND INITIAL CONCLUSIONS

We believe that the following is likely to benefit savers with small pots:

- Review and agree assumptions for a small pots ecosystem and develop high-level process maps for both “push” and “pull” models.

FURTHER EVIDENTIAL NEEDS

- Review small pots process flows in other countries, for example, Australia.

CHAPTER 3: POTS AND FUNDS IN SCOPE

SUMMARY

- The Co-ordination Group has drawn initial conclusions about the pots that should be considered as in scope for the purposes of further analysis of small pots solutions. This can be summarised as small, deferred pots held within a default arrangement under a qualifying scheme. (The definition of a deferred pot is complex, and no firm conclusions have yet been drawn.)
- Consideration has also been given to Sharia- compliant and ethical funds, and future needs to assess other kinds of funds has been identified.
- A staged rollout to slowly increase the pots funds in scope has been identified as potentially beneficial; it should be considered alongside other initial recommendations on scope in the future.

Building on the assumptions outlined by the Co-ordination Group (above), further consideration has been given to begin to define which pots should be in scope for an automatic small pots solution with a view to was maximising benefits for savers, minimising saver detriment and maximising efficiency savings across auto-enrolment schemes. Work will need to continue to refine the scope of the ultimate consolidation model and to assess the impact this will have on savers and the automatic enrolment market.

INVESTMENT CHOICES

In order to minimise consumer detriment, the Group has agreed that the focus of work should be on small deferred pots held within the default fund of qualifying schemes on the basis that:

- These pots will all be subject to the charge cap
- The objectives of default funds across qualifying schemes are broadly comparable (certainly more so than those of self-select funds)
- Most members with small pots in a default fund will not have made an active choice to be in that fund.

Therefore, pots in scope could be defined as small-deferred pots held within a 'default arrangement' under a qualifying scheme for the purposes of:

- **Regulation 3(1) of the Charges and Governance Regulations 2015**
  (i.e. a default arrangement under a qualifying occupational money purchase scheme (or money purchase section of a hybrid scheme)), or
- **The Personal Pension Schemes (Restrictions on Charges) Instrument 2015**
  (i.e. a default arrangement under a qualifying personal pension scheme or stakeholder pension scheme).

This would mean that where a saver has chosen to invest their savings in a scheme's self-select investment fund their pot would not be in scope for automatic transfer even if it fell below the applicable small pot value threshold (subject to the potential inclusion of small pots held within Sharia funds which is discussed below).

It is recognised that a minority of savers may have made an active choice to be in their scheme's default fund. However, it would be impracticable for providers to identify such members and, in any event, if their pot were transferred it would be transferred into a broadly comparable default fund within the receiving scheme.

Savers may also have taken other actions or made other decisions in relation to their deferred pot, such as:

- nominating a beneficiary or beneficiaries, or
- changing their expected retirement age.

However, the Group does not consider that such actions should prevent a saver's pot from being included as part of an automatic transfer framework.

Alongside small pots held within the default fund, the Group recognises that there may be a case for including small pots within Sharia funds in any automatic transfer regime on the basis that for some members the Sharia fund is equivalent to a scheme's default fund (as it is the only fund in which they would be happy to invest) and Sharia funds may be comparable between different schemes (although it is important to recognise that they are not all equally acceptable to different communities). Excluding small pots within Sharia funds might also be open to challenge on equal treatment grounds. If Sharia funds were in scope, it is recognised that small pots within such funds would need to be transferred into another Sharia fund within the receiving scheme.

The Group has also considered whether small pots held in ethical funds (not in a default arrangement) should be in scope. However, the Group considers that they should not be included on the basis that there is too much variation between such funds and the question of what constitutes an ethical fund is more subjective. In most cases, ethics will also not be considered to be a protected characteristic for the purpose of any future Government Equalities assessments. Over time, ethical and self-selected funds could become part of a legislated-for small pots solution.

Further evidence is needed on the proportion of small pots within self-selected funds and ethical funds now and over time, and the methods for dealing with gated funds where automatic transfer models are pursued. Thought will also need to be given where newer or otherwise different self-selected funds are held from those that were previously available, which may be another reason to suggest there is merit in different consideration for 'stock' small pots and 'flow' small pots solutions.

WHAT IS A DEFERRED POT?

The Group has discussed when a small pot might be considered to be a deferred pot and, therefore, eligible to be automatically transferred. A number of different trigger events have been considered:

- no employer or member contributions being paid into the fund within a prescribed period (such as six months or a year)
- the existence of a new active pot, or
- a saver leaving employment.

The first of these options may be the simplest to administer on the basis that it ought to be relatively straightforward for schemes and providers to identify when no contributions have been paid into a pot within the relevant period. However, an issue that would need to be addressed if this trigger is used is how it might impact:

- savers who have decided to stop contributing for a temporary period, or
- savers who are not contributing as a result of being on family leave or who take a sabbatical or a career break.

In most instances, it is unlikely that a saver would have a current active pot in these circumstances. Therefore, a saver's deferred pot would not be transferred (even if it was a small pot) under any model which only provided for transfers to be made into a saver's current active pot. However, if the final model provides for the consolidation of two or more small deferred pots or for small deferred pots to be transferred into a consolidator there would need to be some way of identifying savers whose pots are not truly 'deferred'. One way in which this could be done is via a new opt-out and request to cease contributions process where savers could stop the small deferred pot being transferred. However, this would not necessarily identify all savers who have temporarily stopped contributing to their current pension pot.

The second trigger also has some merits. However, it is unclear how a provider would know that a saver has a new active pot. The fact that someone has started contributing to a new active pot also does not automatically mean that their existing pot(s) is deferred (for example, a saver may have multiple jobs or may be taking a temporary break from paying into their other pot(s)). It would also need to be determined whether consolidation happens immediately following the creation of a new active pot or only after the saver has been contributing for a minimum period or where the value of the savings in the new pot have reached a prescribed level. Where a saver has multiple jobs and multiple active pots it would also need to be determined which active pot any small deferred pots are paid into.

On the face of it, the final trigger above may also have some merits, but this information is currently not available to pension providers in most instances. As above, it would also need to be determined whether consolidation happens immediately or only after a saver has been in their new job and been paying into their new employer's scheme for a minimum period or where their savings in that scheme have reached a prescribed level. The same issues associated with savers with multiple jobs would also need to be addressed.

There are risks to accidentally moving deferred pots, for example, it may mean that an employer is in breach of their automatic enrolment duty. Ways of dealing with and remedying incorrect transfers need to be developed. The opt-out process and the member communications associated with this will be important in mitigating the risk of a deferred pot being wrongly identified as being in scope. However, they cannot be expected to prevent every potential incorrect transfer.

On balance, it is likely that prescribing a time period after which a pot is deemed to be a deferred pot if no further employer or member contributions are paid into it will be the best trigger event. However, it is recognised that the most suitable trigger event may be model dependent and, particularly, whether that model is fundamentally designed on a 'push' or 'pull' basis. For example, different triggers may be more appropriate for pot follows member compared to a default consolidator model, therefore, the definition of a deferred pot will need to be considered within the context of the relevant model once a preferred solution has been identified.

The choice of trigger event(s) and their impact should also be considered as part of the consumer journey research and labour market analysis so that their impact can be more fully understood.

INITIAL CONCLUSIONS SUGGEST STAGING ROLLOUT MAY BE BENEFICIAL

The Group considers that it is likely that it will be necessary to adopt a phased roll-out of any automatic transfer solution in order to minimise any potential member detriment and recognising the time it will take for different schemes to prepare for this.

It is envisaged that the first phase could cover small pots held within authorised master trusts and contact-based workplace pension schemes used for automatic enrolment. This could then be extended to cover small pots held within other workplace pensions schemes that are used as automatic enrolment schemes (such as employer operated money purchase occupational pension schemes).

For staging to be successful, further engagement with the wider industry would be needed to make it work. The Staging process will also need to be considered in the context of the automatic small pots solution. Staging might be able to occur faster, or slower, depending on the model. The Group has suggested starting with lower sized small deferred pots and increasing over time, which necessarily limits the range of small pots that are within scope of an automatic transfer solution initially.

Introducing an industry-wide automatic small pots transfer solution will require legislation, as the industry can only go so far within the current legislative context to resolve the small pots problem. This report highlights a number of areas where government intervention will be needed in order to make progress.

In advance of any legislative compulsory transfer framework, it could be helpful to have assurance or a statement from the Regulator to facilitate small pots transfers. As we are exploring the opportunity for transferring and consolidating small deferred pots in the automatic enrolment market, and as currently we believe the balance of small deferred pots reside in automatic enrolment master trusts, the Member Exchange pilot (Chapter 7) will inform the extent to which transferring and consolidating small deferred pots is feasible within existing legislation and current trustee comfort. It is possible that the pilot, or other work, will identify the degree to which helpful assurance could be provided by the Pensions Regulator to deliver additional comfort for trustees and relevant parties to facilitate small deferred pot transfers.

Any such assurance from the Regulator should therefore be intended to help give some comfort to trustees in the short and medium term and could help unlock solutions that could work for 'stock' pots. The Regulator may, for example, be able to provide a statement highlighting the holistic approach trustees must take, including the benefit to members of having fewer small, deferred pots. This is notwithstanding that the statement will be unlikely to establish rights savers have in the case of transfers they are not happy with (Chapter 4) or assert which schemes offer relative value for money. Particularly, some reassurance could be provided by Regulators and Government that new scams and other legislation should not be a barrier to transfers to Master Trusts (Chapter 8). The Group will continue to consider the need for supportive contributions in the next stage of the work.

Even if member exchange is successful in achieving a meaningful level of small pot consolidation, it might also lead to distortions in the auto-enrolment market as it would mean that some schemes and providers can relieve themselves of small deferred pots (at least to some extent) whereas other cannot. For example NEST, like the contract-based auto-enrolment schemes, is unable to undertake member exchange within their current framework, as they cannot undertake bulk transfers without consent. However, the degree of this distortion will depend on the scale and nature of small deferred pots held in the trust-based sector compared to in contract-based sector.

NEXT STEPS AND INITIAL CONCLUSIONS

We believe the following are likely to benefit savers with small pots:

- Pots within scope of future automatic transfers should be:
  - Small deferred pots within default funds and Sharia funds under qualifying schemes.
  - A suitable trigger for identifying a deferred pot and when it can be transferred needs to be considered further in the context of different consolidation models and as part of the consumer journey research and labour market analysis.
- Implementation of a small pots solution should be staged, starting with what is possible within the current confines of existing legislation.
- Once further model design work is undertaken, the pots in scope should be modelled against them to assess the impact on savers and the automatic enrolment market.

CHAPTER 4: DATA MATCHING

SUMMARY

- Assessment of existing data requirements and the implications for matching protocols show that various options remain for small pots solutions. However, it appears clear that 'raising the bar' for matching standards may well improve protections for savers from errors in some cases, but will also reduce the number of positive matches available for potential automatic transfer.
- Data availability and quality are identified as unexpected key issues in data matching for small pots and the importance of these factors in making progress on administrative issues should not be underestimated.
- The recommended next phase should consider the implications for potential industry wide data matching standards.

The DWP Chaired Small Pots Working Group recommended that[25]:

> *"Developing and testing data that would provide sufficient matching capability, compliant with data sharing legislation, (as a proxy for a unique reference) to verify the identity of the person whose pot(s) will be transferred is the same as the identity of the person whose pot will receive the transfer. Opportunities to build out from data-matching in relation to Pensions Dashboards; the PPI's work on the Pensions Data Project and industry good practice should be maximised."*

The 'heart' of data standards for small pots solutions will be data matching. Discussions have therefore focused primarily on this topic. As laid out in the previous Small Pots Working Group report, it is important to leverage other data matching work. This Chapter considers matching criteria used across a number of different initiatives, specific needs for small pots data matching and current research on data accuracy and matching.

CURRENT INDUSTRY DATA MATCHING

The table below considers matching criteria across a number of different initiatives:

INITIATIVE	DESCRIPTION	APPROACH TO DATA MATCHING
Pensions Policy Institute (PPI) Data Project	Research-driven initiative to answer such questions as "How many DC pension pots, on average, do UK workers have?" and "How much are the pots currently worth?". Within the research database, individuals' records will be matched, aggregated and anonymised.	The aim is to start testing in 2021, matching only on National Insurance Number (NINo) & Date of Birth (DOB), accepting that using just these two items will result in some false positives and false negatives. For a research database, a small proportion of false matches is not felt to be a serious issue. Hashed Surname and Postcode data may also be supplied by the five participating pension providers, but not used for matching, so there will be learnings on these two items too.

25 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf

INITIATIVE	DESCRIPTION	APPROACH TO DATA MATCHING
Pensions Dashboards Programme (PDP)	Dashboards will be a "pull" service, i.e. individuals ask for, and consent to, their pensions being found. However, Dashboards and small pots "false positives" are both such highly undesirable outcomes that the challenges of matching for Dashboards and small pots do largely overlap.	The initial version of the PDP Data Standards Guide, published in Dec 2020, lists the "Find" personal data items which will be passed to the pensions industry for them to use for matching. In its Call for Input (CfI) on data standards in July & August 2020, the Pensions Dashboards Programme (PDP) asked industry participants a series of questions, including: *"Which data items do you anticipate could be used to definitively match individuals to their pension entitlements?"* A summary of the 61 responses to the CfI received[26] was published in October 2020. It will be up to each pension scheme / provider to choose which of the "Find" personal data items it will use to match against its pension records. In July 2021, PASA announced it will be working with the ABI and PLSA and 11 leading pensions administration software providers to devise a consistent suite of Data Matching Conventions (DMCs). Pension schemes and providers will be able to choose which DMC(s) they wish to use (unless they wish to specify their own). Initial DMCs are targeted to be ready for alpha Dashboards testing by the end of 2021.

26 https://www.pensionsdashboardsprogramme.org.uk/2020/10/28/responses-to-call-for-input-on-data-standards/

INITIATIVE	DESCRIPTION	APPROACH TO DATA MATCHING
DWP 2015 Automatic Transfers / Pot Follows Member (PFM) initiative	The Coalition Government did considerable work on automatic transfers, including legislation to facilitate them in the Pensions Act 2014, before the policy was "parked" after the 2015 General Election.	The DWP framework document for automatic transfers, published in Feb 2015, sets out a matching approach. Chapter 4, paragraphs 11-14, in the framework document cover matching, in particular the key observation that: "There is a balance to be struck between generating the maximum number of matches and avoiding erroneous matches." To strike a good balance, the framework proposes that a positive match should only be deemed when: NINo matches (identifying null, dummy and temp NINos) and DOB matches and at least two of the following match: Initial (felt to be very much weaker than First Name) Surname Gender Also consider Postcode and Mobile phone number. Bear in mind, Mobile phone number is not a 'usual' data field for pension schemes.

In summary, across the various different types of organisation in the UK pensions administration industry, NINo and DOB are seen as key matching elements. Despite this, neither NINo nor DOB are without issues. Surname, First Name (or Initial), and Postcode are also seen as very important, but less consistently so across all parts of the industry.

SMALL POTS DATA MATCHING REQUIREMENTS

From the above narrative, we can see there is a difference in matching requirements; those which will have input from the saver and those with no input. For example, Dashboards may have a route to check "maybe matches" and follow up with savers to check details. This would not be the case with an auto-transfer. This will impact on the criteria set for matches.

For example, automatic small pots transfers should aim for a 'high bar' of accuracy to ensure incorrect auto-transfers are rare. Whereas, for other matching purposes (for example, research) it is more acceptable to have an element of mismatching as this is less crucial.

For automatic transfers, the key question is: what, as an industry (and Government), do we feel is an acceptable match rate for auto-transfers:

- If the match bar is set very high, we can be certain no incorrect auto-transfers will ever be made, but there will be a reduced percentage of successful automatic matches made, and thus fewer small pots will be consolidated. The balance to this risk is if a small pot is left, it is likely to be eroded by charges (see Chapter 1).
- If the match bar is set lower, there may be a risk of incorrect auto-transfers sometimes occurring, but there will be higher percentage of small pots being consolidated. The risk of fraud might also be increased (where an 'allow/deny list' system is not used), but the amounts will be very small so the cost of repatriation at a later date may be very low too. A high number of mis-matches may also result in a loss of confidence in the system which would be damaging.

Further research is needed to understand what the likely error rate will be. Some of this will be gained when matches start to occur through Dashboards with real data. Other evidence, albeit very limited because of the approach being taken, will be gathered through the pensions data project.

The population of individuals who are likely to be subject to auto-transfers is highly likely to be different to those who will engage with Dashboards i.e. by their nature, unengaged versus engaged individuals. However, over time a successful rollout should mean that many 'disengaged' users will eventually use pensions dashboard. At worst, it is possible that if incorrect auto-transfers take place, unengaged individuals may not find out their pot has been automatically transferred. By restricting automatic transfer to small pots and having an opt-out process and communications, this will help to mitigate this risk and limit the value of any pots being incorrectly transferred. This is also important to consider when looking at the likelihood of mismatches and an acceptable error rate.

We need to learn more about the actual accuracy of personal data items held by pension schemes and providers. This will enable the industry to set a realistic 'percentage match ambition' for automatic transfers. This match ambition should be designed to be acceptable to both industry participants and members / consumers.

The project also needs to identify the GDPR implications of acting on an incorrect transfer as a result of a false positive, as this may include fines on the participants involved which could be substantially higher than the mere cost of re-instating records that were incorrectly transferred to a different (and incorrect match) person.

MANAGING/MITIGATING DATA MATCHING RISK

As discussed, some element of mismatching is likely to occur in any automated model. Further discussion is needed on whether the ceding or receiving scheme should be liable to 'put right' a transfer to members in the event of a false positive and transfer; or whether a shared liability model should be taken forward. Similarly, the interaction with any member opt out should be taken into account. Research should be undertaken to understand how this problem is tackled in similar markets, e.g. authorised, and unauthorised push payments, and other jurisdictions.

However, regardless of where liability falls, the Group has so far concluded that the following protections should be considered as appropriate to put in place for members:

- There should be no time limit 'putting transfers right' for members.
- A member should be 'put right' (i.e. compensated for the full lost value of the pot including missed investment growth).
- The member with incorrectly allocated funds should not have money clawed back from them. However, this could depend on the amount of time taken to spot the error, for example, if within 12-24 months it may be possible to justify correcting the error.
- Further consideration is needed on how members would be compensated and the principle of 'restored rights' found elsewhere in pensions. In a small pots context, this may be disproportionate and therefore savers could be compensated with cash rather than through unwinding transactions and/or investments and therefore truly returning savers to the exact position they were in previous to the transfer.

- Where errors are not identified for a number of years, consideration of how savers' pots could be 'put right' and what is appropriate and proportionate in the small pots context is needed.

Both liability and compensation models will need further consideration, not least to establish how the net cost of each approach could impact on the overall efficiency of the proposed solution.

RESEARCH ON DATA MATCHING

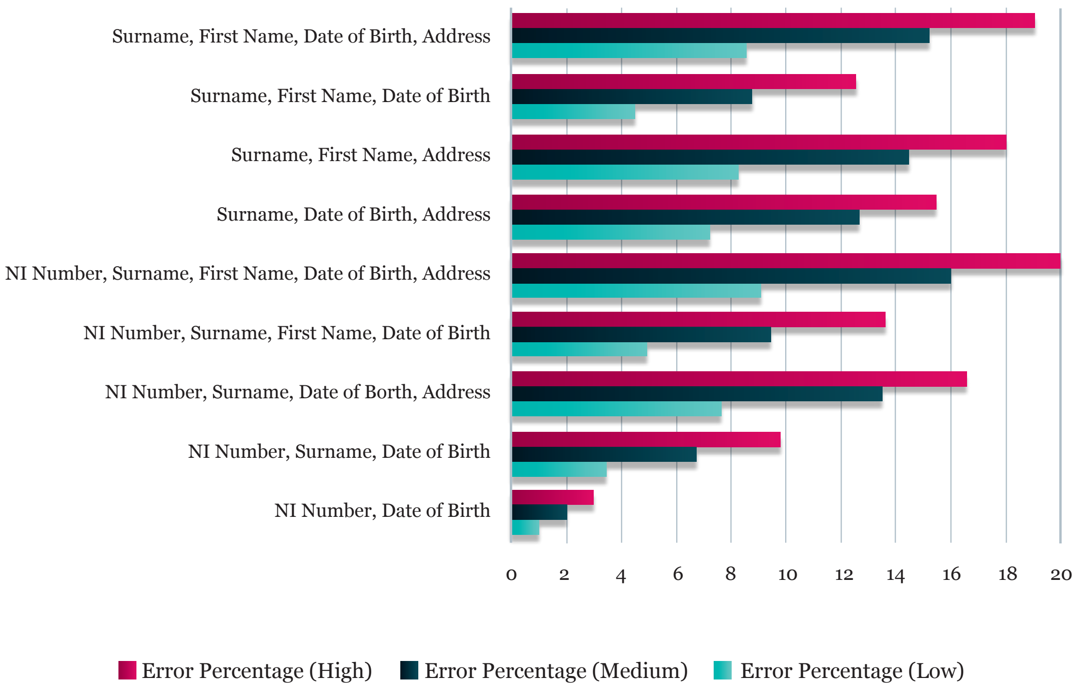
Small Pots Big Solutions[27]: Exploring the tightrope of data matching – itm

ITM conducted analysis on real scheme data to look at how effective different matching criteria are for finding all pension records belonging to an individual and for preventing mismatches that lead to incorrect pot transfers[28].

The findings from this research were that the more data items that are included in matching criteria, the greater the chance that poor data quality will mean a match does not occur. There is also a reduced chance of a match where there is the inclusion of data items in matching criteria that are subject to more frequent change (such as address), and are hence more prone to inaccuracy.

The graph below shows these results across a range of potential matching criteria:

PROBABILITY OF LOST OPPORTUNITY



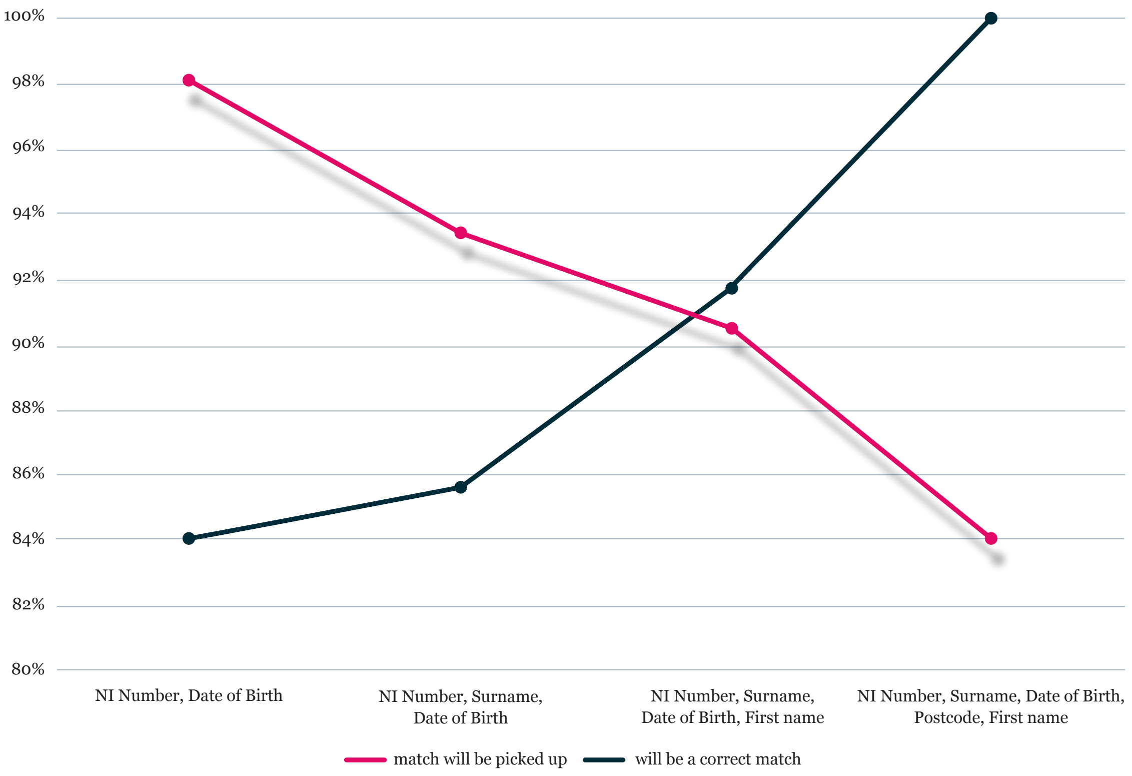
The research also found that no single matching criteria can achieve close to 100% on both its ability to identify true matches (which is driven by the "sensitivity" of the matching test) and its ability to avoid mismatches (which is driven by the "specificity" of the matching test), and that small changes can result in large deviations from 100%.

27 https://www.plsa.co.uk/Portals/0/Documents/Thought-Leadership-Documents/2021/The-Idea-Series-Small-Pots-Big-Solutions.pdf?ver=a027aN-l83QOLotRsdXtNDg%3D%3D

28 https://www.plsa.co.uk/Policy-and-Research/Thought-Leadership-Library/The-Idea-Series-Small-Pots-Big-Solutions

The graph below shows the effectiveness of four of the different matching criteria - for each one showing an estimate of the probability that a match made will be a correct match (black line) and also the probability that a correct match *will actually be picked up* and will not be prevented by poor data quality (red line).

EFFECTIVENESS OF MATCHING CRITERIA



For example, the second tightest criteria (i.e. second least likely to make an incorrect match) of Date of birth, NI number, Surname and First name, has scores of 91.6% and 90.5% respectively. Forming conclusions on what this means for the likelihood of mismatches in the real world is statistically challenging, anything like a 9% chance of a mismatch may be too high to provide the required assurance for automatic small pots solutions.

We understand that further research is being planned to refine the picture and reduce the reliance on assumptions.

Pensions Dashboards Programme (PDP) research

In addition to the above, the PDP's qualitative data research with pension schemes / providers[29] undertaken by PwC in the Summer of 2020 and published in October 2020, found:

> *"[The 15 research] Participants are regularly testing the key data required to match individuals and most are confident about the quality of this information. However, any assessments are based upon the data being present and reasonable [as opposed to being accurate].*
>
> *Data accuracy relies on the third parties [such as employers, previous administrators, etc.] providing the information in the first place and keeping it up to date, therefore the true extent of the challenges faced by key identifier data may only become apparent when data providers test data with the pensions Dashboards ecosystem."*

The research found that after an employee has left service, their employer no longer contributes to keeping their record up to date.

29 https://www.pensionsDashboardsprogramme.org.uk/2020/10/28/pwc-research-pension-providers-and-schemes/

DATA QUALITY

Good data quality is crucial for any small pots solution. As identified in the research above, poor data quality can result in missed opportunities for pot consolidation. We do know that there are some issues with poor data quality in schemes. A 2020 TPR research report with DC schemes found that [30] approaching one in 10 schemes (8%) had identified data quality issues in the last two years. This proportion increased to 29% of medium schemes, 33% of large schemes and 50% of master trusts.

Poor data accuracy is compounded by poor third party performance. Anecdotal evidence suggests even when the pension fund prompts employers to resolve a data mismatch they rarely correct their own source systems, leading to further use of the wrong/out of date data.

For small pots this is important as knowing data is present but potentially inaccurate increases the risks of incorrect matching and particularly false negatives (or "missed opportunity matches"). Employers are known to use reasonable but wrong data to get through the contribution input process, which will later need to be corrected by the scheme.

Improved data quality is not always in the control of pensions providers. Providers are reliant on employers to provide correct data and on savers to keep it up to date. Similarly, employers are reliant on employees providing them this correct data. Schemes can only run on the data they are given.

Early on-boarding of certain schemes to pensions Dashboards will undoubtedly be an important test of matching and will feed into the small pots matching approach. However, it is unlikely to be a full and complete test of the challenges of matching. Real life "Find" testing will not happen until the Beta phase, but there are limits to how much this will truly act as a test of matching approaches if the testing is restricted to a relatively small number of schemes as expected. The real test to matching will come from widespread consumer use of dashboards.

Providers and employers should work together to improve their data quality in general within given limitations, but particularly in advance of Dashboards and to support small pots consolidation. Government may also have a role to play in improving data. For example, they could help with verifying savers details to ensure they are correct, for instance verifying that the NINo is correct[31]. Improvements in employment administration and payroll procedures when onboarding employees may also help improve data held by schemes.

FIND MECHANISM

In order for matching to occur, a 'find' function may be needed to locate small pots within other schemes (depending on the model that is eventually selected). Dashboards functionality is a start point for this purpose, but further investigation and development is needed.

INDUSTRY WIDE UNIQUE IDENTIFIER

The 2020 DWP-Chaired Small Pots Working Group report discussed the potential pros and cons of a new unique identifier, as international evidence suggested that a genuinely unique identifier was a pre-requisite to success for pot consolidation in certain countries. A PPI report looking at how other countries have dealt with small, deferred pension pots also previously found that without a unique identifier, centralised transfer and consolidation systems were less effective[32].

30 https://www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/dc-research-summary-report-2020.ashx

31 HMRC already have services, such as the NINo helpline.

32 https://www.pensionspolicyinstitute.org.uk/media/3691/20210112-ppi-small-pots-international-report-final.pdf

There are known errors with NINo in pension schemes, which may make it unsuitable to use as a unique identifier. For example, NINo is not considered as an identity number by government; it is an internal number used by HMRC and DWP and should not be used as a proof of ID or right to work [33]. However, an individual's NINo should be unique, although some are reused. The employer does have a role in correcting and providing correct NINos to pension providers. The Group has identified that further evidence on NINo, particularly the proportion of errors and where they are occurring in the process, is required to understand how robust this is to use as a unique identifier. It is worth noting that even a "unique identifier" could end up being non-unique due to data entry errors.

There are limitations with a unique identifier, for example, it may not help to resolve the stock of small pots if they cannot be matched to newer pots with a unique ID. However, once allocated it could help with future pension provision. A PPI report [34] also identified challenges with a unique identifier:

- It would take several years to develop. Time and resources would need to be invested for its development.
- They are not always completely secure and could raise data privacy issues.

Progress on resolving small pots can be made without the creation of an unique identifier, although it will be important to understand the reliability of matches using existing data criteria. The future use of industry-wide unique identifiers on a consistent basis would be hugely helpful for the industry to get a handle on these issues for new pension pots (i.e. the flow of small pots) where lessons cannot be learned from dealing with 'stock' pots, and a centralised or national unique identification number would be ideal for this purpose. However, further understanding is needed on how far a unique identifier can overcome some of the inefficiencies with existing data and it would not be immediately helpful in resolving the stock of small pots.

To address existing pension pots data providers (such as ISPs) may be able to create their own person identifiers to record individuals who are found to exist multiple times in one arrangement, or across different arrangements connecting through that provider/ISP, once those matches have been made. These person identifiers could easily be matched to a new centralised ID number in the future, if one is available, but would benefit the matching process in the meantime. However, there are GDPR considerations that need to be investigated.

33 https://researchbriefings.files.parliament.uk/documents/SN04281/SN04281.pdf; https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/581216/National_Insurance_number_confirmation_research.pdf ; https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/populationestimates/methodologies/nationalinsurancenumberNINodataqualityassuranceofadministrativedatausedinpopulationstatisticsjan2017

34 https://www.pensionspolicyinstitute.org.uk/media/3694/20210112-ppi-small-pots-international-report-final.pdf

NEXT STEPS AND INITIAL CONCLUSIONS

We believe that the following are likely to benefit savers with small pots:

- Small pots data matching protocols align with those for Pensions Dashboards and should be considered as part of the ongoing work by PASA, PLSA and ABI on Pensions Dashboards Data Matching Conventions (DMCs), whilst recognising that the different context of small pots consolidation may require stricter criteria.
- Further understanding of the reliability of matches using existing data criteria and understanding how far a unique identifier can overcome some of the inefficiencies with existing data.
- Providers work with employers and government to improve data quality, where they are able to, for example, government could help to verify data held by schemes. Particular focus should be placed on the need to provide sufficient data for effective member matching as part of employee set up.
- Ensure that the current phase of industry development supporting Pensions Dashboards, such as the design and build of ISP services, is informed and aware of the future matching requirements of Small Pots.

FURTHER EVIDENTIAL NEEDS

- More detail on other countries' experience on how their respective systems are set up e.g. liability models.
- Further understanding on the reliability of the NINo to be used for matching and, particularly, whether the reliability differs for 'stock' pots (those that are already in the system) or 'flow' pots (those that occur over time or have yet to occur).
- Likely error rates of matching:
  - Matching, and understanding the likely error rates of different options, and deciding acceptable practices/procedures where an error occurs.
  - The life journey of NINo and where errors are arising.
- More detail on other countries' experience on how their respective systems are set up e.g. liability models.
- Further consideration of liability and compensation models.

CHAPTER 5: LOW-COST TRANSFERS

SUMMARY

- The current individual member-initiated transfer process has been mapped to identify where costs occur and discover potential efficiencies. Low-cost transfers are a necessary condition of progressing small pot consolidation models in more detail as without these the net gain for savers from consolidation is likely to be severely curtailed.
- The conditions for any future small pots transfer process have been considered. Notably a potential 'triage stage' has been proposed to 'screen out' small pots that are not in scope of small pots transfer models, which would enable more efficient procedures to be followed from that point onwards. Communications must also be digital. The first model requirements have been assessed, such as opt outs and compulsion, and further areas for assessment identified.
- Key barriers for Low-cost transfers have been identified including those that are legislative and regulatory, and recommendations made to reduce these.

The Small Pots Working Group report recommended that the industry should:

- Identify requirements for a low-cost bulk transfer process; and
- Conduct an end-to-end review of the current individual transfer process to identify where costs occur and where they can be removed.

It was also highlighted that mass transfers which are non-member led may necessitate new approaches to achieve low-cost delivery, while maintaining proportionate safeguards for members. This mass transfer system would be needed for any large-scale consolidation process for small deferred pots. Making progress towards a more efficient and cheaper transfer process is necessary for any of the proposed automatic transfer solutions to the small pot problem.

MAPPING CURRENT PROCESS

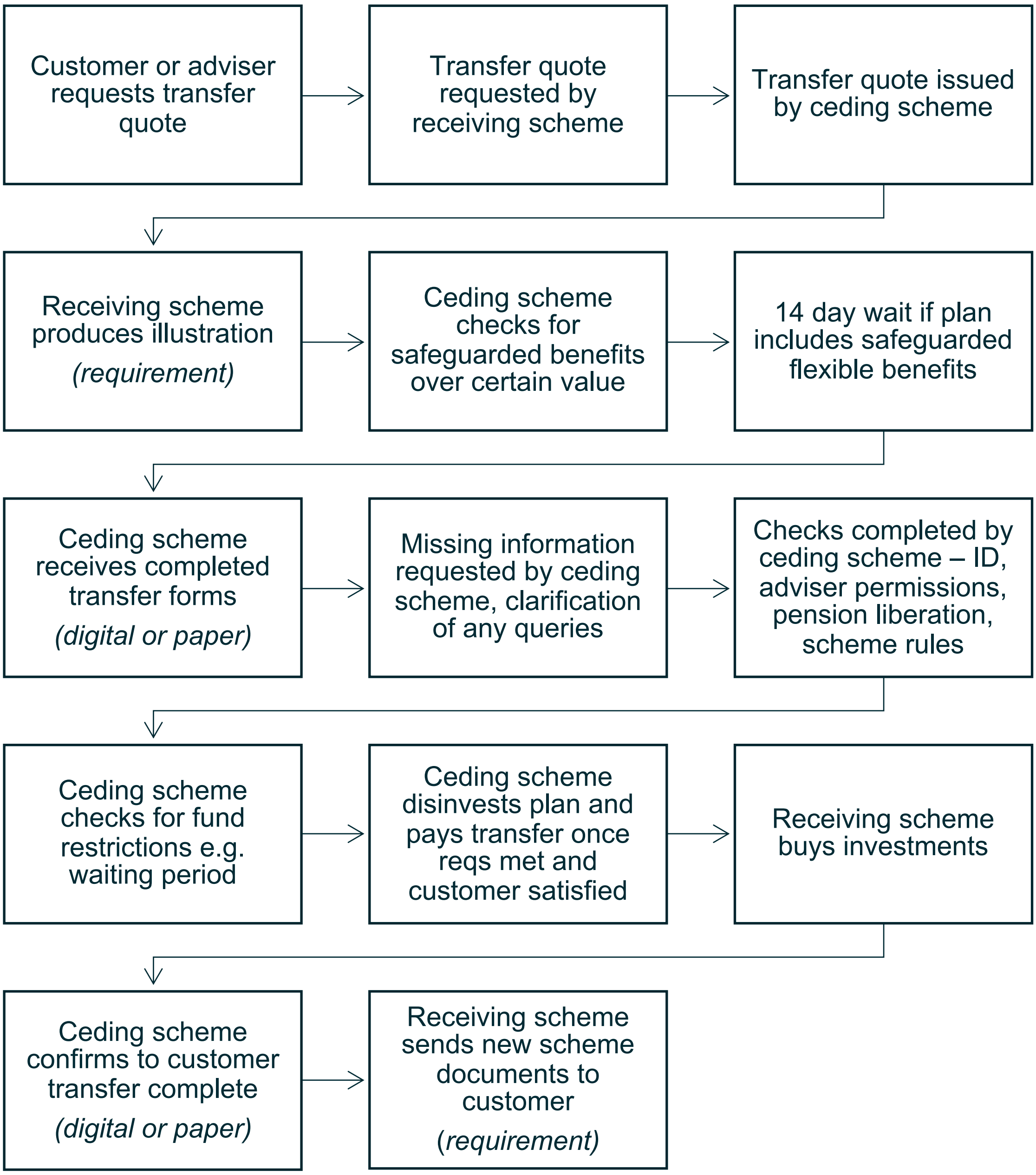
The group mapped out the current member-initiated transfer process, amalgamating firms' individual processes. Costs of transfers are made up of three elements:

- Cost of payment (BACS, CHAPS or faster payments)
- Transfer technology provider costs
- Core administration of provider

On the first, the cost of payment is known and not controllable, although there is now greater use of faster payments which are typically cheaper. On the second, there are a number of transfer service providers in the market and are commonly used by pension providers, although not all providers pay for and utilise the fully automated services available.

The core administration of providers facilitating small pots transfers are where the group has focussed its efforts. End-to-end integration of pension provider and transfer service provider systems is possible but requires substantial upfront investment; legacy systems and multiple provider books also act as significant barriers.

Figure A: Simplified Transfer process map – member-initiated transfer
(for a contract-based transfer there are no illustration requirements or specific post sale requirements for transfers to OPS)



CURRENT COSTS IN THE PROCESS - WITHIN INDIVIDUAL PROVIDERS/SCHEMES

PROVIDER/SCHEME	▶ Receiving provider: • Communications to member and ceding provider • Matching money to customer • Investment of funds ▶ Ceding provider: • Providing transfer value • Disinvestment of assets • Transfer of money to receiving scheme • Communications costs Cost reduction has been realised where processes have been automated. *Barriers to cost realisation/same provider consolidation* ▶ Where there are multiple books of business. There will be several administration functions in operation that cater to different schemes of varying maturity. Particularly in contract-based arrangements, it is common for employer schemes to have different charge levels and different investment strategies. Bringing these pots together physically would therefore not be possible. Providing joint statements would also be costly, potentially confusing and not possible within the constraints of the simpler annual statement for automatic enrolment busines.
THIRD PARTY REQUIREMENTS	▶ Providers' duties to treat customers fairly and to act in the member's interest leads to due diligence checks and controls on transfers, all of which have a cost attached. ▶ The ceding scheme is expected to undertake due diligence on the receiving scheme. This can take time (and could include cross-checking with HMRC before a payment can be processed). ▶ In contract-based schemes member consent and due diligence before transferring means there often needs to be human input in the transfer process, which has significant costs and seen as unavoidable under the current rules. ▶ Transfers which go through an accepted process take, on average, far less time. Within certain automated transfer solutions providers have already been subjected to a degree of due diligence. *Specific processes that create cost* ▶ Paper-based customer communications. ▶ Customer must review documentation and options. ▶ Ceding scheme must produce customer illustrations. ▶ Administrative checks – for example, verifying customer identification or ensuring paperwork has been fully completed. ▶ Single-employer trust: checking scheme rules for nuances, for example any contractual right to transfer and full or partial transfers. ▶ Master trusts: if applicable, there is an additional process of trustees signing off a transfer. ▶ If independent financial advice is being taken by the customer the provider will need to ascertain whether a customer is still being advised, and if so contact the IFA in question. **All of which are manual processes**. ▶ The level of safeguarded benefits attached to the plan - these can require providers to seek advisor declarations, apply risk warning periods etc. ▶ The time that any transfer value is guaranteed.

EXPECTED CHANGES (CHAPTER 8)	There are several regulatory initiatives in train need to be considered in relation to small pot consolidation. These are: ▸ Expected upcoming pension scam transfer regulation. ▸ Normal Minimum Pension Age change to 57 - protected retirement ages. ▸ FCA and DWP requirements on "Stronger nudge". ▸ Rules on de minimis charging of small pots.
POTENTIAL NEW COSTS IN AN AUTOMATIC TRANSFER SOLUTION	▸ Checks that a pot is suitable for automatic transfer e.g. that the value is less than a certain size and it has no guarantees. ▸ Providers to check for protection such as protected tax free cash or early retirement ages that would be lost on an individual transfer, and make sure the member is informed beforehand. ▸ Use of pension finder service.

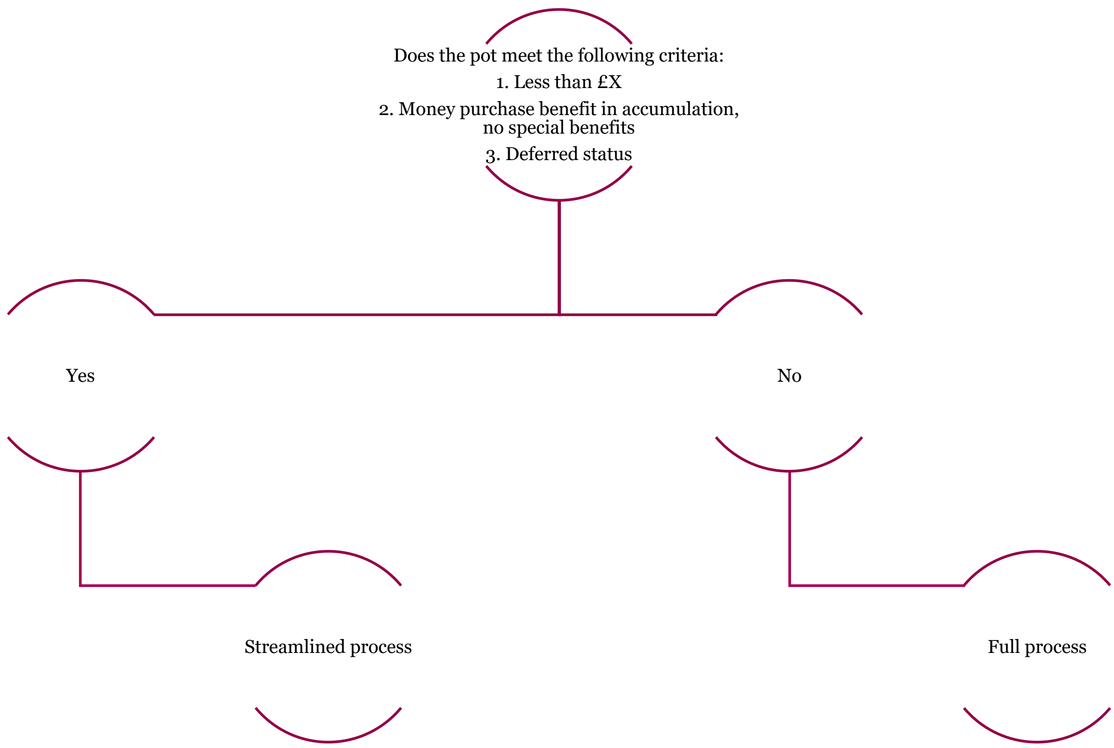
The group considered what changes could be made to adapt the current process to make it more economical to transfer member-initiated small pot transfers, and to help facilitate potential future automatic small pot transfers.

The simplified transfer map in Figure A includes steps which are taken for benefit types beyond the small pots scope (e.g. those with safeguarded benefits), but have been included for completeness. Some steps are unavoidable – such as disinvestment/reinvestment of funds. Some manual processes that lead to increased transfer costs could be circumvented by removal of certain due diligence where the receiving scheme is trusted, and moving from paper-based communications to digital communications

Triage stage

The group discussed a "triage" process that would identify simple automatic enrolment pots, without guarantees, that are under an agreed defined small pot threshold (for further discussion of the working assumptions the Group has been using please refer to Chapter 2). These pots would then move through a more streamlined process where the ceding and receiving provider would not be required to undergo some of the processes under a risk assessment. Implementing this stage would require a rules engine in order to determine which pots meet the requirements. This would help lower costs and improve efficiency for transfers both within and out of an automatic transfer process.

Figure B: Proposed triage assessment



Much of bringing down the cost of small pot transfers relies on taking out certain costly steps from the existing process. Given the proposed "triage" step this would allow the existing checks on guarantees to be taken out of the process as any pots with these will have been screened out already. Other steps include:

- The group considered that some regulatory requirements, such as the FCA COBS 13.1 on pre-sale illustrations and the legislation for statutory money purchase illustrations (SMPI), for very small pots could be seen as disproportionate (and may also need to be changed were automatic transfer solutions to be explored).
- Where documents do need to be sent to customers, this should be done digitally. For example, the requirements telling the customer that their pot has been moved would need to be digitised in order to avoid the associated cost of paper-based communications.
- In the current process there is a step requesting further information from the ceding provider, in a fully automated system this step would no longer be needed as the full information is exchanged at an earlier step, or if automatic transfers were to occur this could include only a defined list of providers.

BARRIERS TO DIGITAL COMMUNICATIONS

Providers will not necessarily have an email address of the scheme member (unless previously requested during the transfer process), and where they do, it is possible that this is the work email address, and therefore not useful for deferred pots as the member is likely to have moved jobs.

It might be possible to alleviate this problem if all member communications relating to automated transfers are routed through the receiving scheme. However, it might persist to be a problem if small pot-generative employers, for example those in hospitality and seasonal work do not end up giving workers email addresses. This reflects the general difficulty with all forms of contact including address accuracy. While the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010 regulations require a member's email address to be shared with a pension provider "where the employer holds this information", the Pensions Regulator's guidance on record keeping does not include this requirement [35].

This group has considered changes to the legislation but concluded that more work needs to be done in finding a solution to the problem of poor member contact data. Initially the group proposed removing the caveat in the legislation so that a personal email must be provided but realised this is not a panacea. There will be people who are not happy giving their personal contact details to their employer and email is problematic as a form of communication as people have multiple email addresses and stop using older addresses as they move through life. If members fail to understand the importance of receiving pension communications, they are likely to provide email addresses they do not use and therefore will not receive them.

The group further agreed that any change to the legislation should avoid referencing specific communication technology to make sure it is future proofed. In addition, it noted that placing a requirement on trustees and pension providers to hold employee personal contact information does not solve the problem of employers failing to collect or share this information. Therefore, it was the view of the group that creating an additional requirement around email addresses would not necessarily be deliverable. Furthermore, this approach would be aimed at preventing future information shortages but will not be beneficial for existing pots as it is difficult to go back and fill in gaps where contact details are already missing.

IDENTIFYING REQUIREMENTS OF AN AUTOMATIC TRANSFER SOLUTION

Third party services

Third party services are commonly used by pension providers when making transfers, however, the working group has heard from participants that their automated capabilities are not currently fully utilised. In the past there has not been a sufficient business case from providers to change internal transfer processes but requiring automatic transfers for small pots could help provide the impetus for providers to do so. Fully utilising the automated aspects of third party services should have the benefit of reducing the time taken for transfers to be processed, as well as reducing the need for costly manual interventions.

35 https://www.thepensionsregulator.gov.uk/en/trustees/managing-db-benefits/governance-and-administration/record-keeping/what-records-to-keep

Looking ahead, implementing automatic transfers for small pots will lead to a substantial increase in the traffic going through third party providers and it is important that further impact assessments are done to understand the market impact of millions of small pot transfers occurring in a short space of time. This will especially be the case to start with as the backlog of small pots are automatically transferred, before the level stabilises at a regular rate as newly deferred pots are transferred. There are already a large number of small pots transfers: one transfer service provider which recorded total pension transfers of £40bn in the year to June 2021 reported that 15.27% of these transfers were pots under £1,000; 47.5% of them were under £10,000 [36].

Further, it will be necessary to take a proportionate approach with incoming scams transfer regulation, nominal minimum pension age checks and stronger nudges. Most providers operating at large volumes should be able to assemble an allow/deny list of trusted receiving schemes, alleviating the issue of scams transfer regulation. Not doing so would call into question the feasibility of delivering a viable automatic transfer process for small pots due to the added expense from the added checks.

Rate of failure

Naturally, there will be some pension pots that fail to make it all the way through either the automated or automatic transfer process. It will be necessary to agree an acceptable rate of failure and a mechanism whereby rejected pots remain where they are.

AUTOMATIC TRANSFER SOLUTION MODEL REQUIREMENTS

Following on from mapping the current transfer process and looking at how it will have to be adapted to allow for a viable automatic transfer process for small pots, the group has set about mapping the theoretical transfer processes for the solutions proposed by DWP's small pots working group report – pot follows member and default consolidator(s) and will be developing this in the coming months. There are some emerging findings that would have implications for the cost of the transfer process that have been laid out below.

Consent and Compulsion

Legislation would be necessary to enable automatic solutions to take place [37], if the costs/benefits work supports this and may be primary or secondary depending on the model that is adopted This includes allowing contract-based providers to move customer money without their consent. The industry view in discussions was that any transfer solution will need to be compulsory (legislation to allow for trustees and contract-based providers) in order to achieve the necessary scale of consolidation and money to ensure that the process is as efficient as possible, particularly be moved where there is might be a risk of detriment. The necessary legislative changes may require either primary or secondary legislation depending on the model that is adopted and the extent to which existing legislation can be used to implement it [38].

Legislative and regulatory compulsion requiring all providers with small pots identified as being in scope to take part in automatic transfers will also be needed. Without it, we would have to rely on a voluntary club where automatic transfers would have to be much more considered leading to a much slower and more costly process. The costs involved in following the existing regulatory processes and ensuring no detriment is likely to make the transfer small pots unworkable regardless of the technology employed.

36 Origo, 2021 – data collection

37 The Pensions Act 2014 provides primary legislation to enable pot follows member.

38 The Pensions Act 2014 provides primary legislation to enable pot follows member.

Opting-out

Just as with automatic enrolment, the automatic transfer of small pots is likely to give customers the right to opt-out if they would rather keep their pot where it is. The Group thought that this option could be presented to savers within existing communications such as the new scheme communications received when starting at a new workplace. This provides the most natural customer journey and avoids unnecessarily creating additional communications which are likely to go unopened or ignored. Furthermore, situating the opt-out choice for automatic transfers within existing automatic enrolment documents will save considerable costs compared with creating separate communications later in the transfer process.

Pensions dashboards interaction

The working group agreed that work on an automatic transfer process must not duplicate the work being done by the Pensions Dashboard Programme (PDP). Where it is possible to have an extension or adaptation that does not compromise the effectiveness of the dashboard initiative this should be sought. The group further agreed that the lesson from the PDP experience was that implementing a new automatic transfer process will have to be a mandatory requirement for providers in order to be successful.

Transfer process

It was recognised that the transfer process might need to be different for transfers to:

- authorised master trusts and schemes operated by FCA providers, and
- transfers to other types of scheme, such as employer operated occupational DC schemes (assuming it is decided that other schemes should be included in scope as potential recipient schemes).

The former (which represents around 80% of transfer that would be taking place) needs to be fully automated whereas the latter could involve more checks on part of ceding scheme (e.g. to prevent transfers to scam arrangements).

As previously highlighted, legislation would be necessary to override the barrier of requiring member consent under contract-based schemes, and for National Employment Savings Trust (Nest) to accept bulk transfers without consent.

Pension scams

For automatic transfers of small pots to be a success, changes to legislation and regulation will be necessary if the emerging evidence on small pot distribution and cost/benefit analysis supports intervention. This includes taking steps to reduce the amount and nature of the due diligence checks required for the automatic transfer of small pots in line with the significantly lower risk of detriment faced with pots of these values and if transfers are only permitted between approved schemes.

A number of the Working Groups have considered the creation of an ‘allow/deny list’ as a helpful component of a small pots ecosystem to mitigate the risk of pension scams. This is on the basis that the risk of scammers infiltrating an automatic small pots solution could be mitigated by limiting the universe of ‘approved’ receiving schemes within any automatic small pots transfer solution. For example, it can be assumed there is zero risk of savers being transferred into a scam arrangement where a small pot is being transferred between two authorised master trusts or FCA regulated contact based pension providers.

It would also reduce the amount of due diligence needed to be conducted by schemes. If extensive due diligence needed to be carried out before a transfer could take place this would undermine the introduction of an automated process, add costs and reduce the scope for efficiency savings. The creation of an ‘allow/deny list’ to allow permitted transfers to proceed automatically with limited checks, would be helpful in lowering the cost of small pot transfers and support an automated solution.

The Co-ordination Group has discussed repurposing the scope of another appropriate regulation intended for the protection of member transfers, such as the four types of entity proposed in the consultation on Occupational and Personal Pension Schemes (Conditions for Transfers) Regulations 2021, to minimise the further due diligence in the event of a member-initiated transfer. Alternatively, a provisional list of schemes could be designed for the specifics of a small pots eco-system to reflect the necessary member protections, and this could include:

1. Public Service Pension Scheme established by The Public Service Pensions Act 2013; or
2. Authorised Master Trusts; or
3. Authorised Collective Money Purchase Schemes (CMPS), when the appropriate regulations come into force; or
4. Workplace contract-based schemes with the requirement to have an Independent Governance Committee

Either of these options could be a reasonable starting point for an 'allow/deny list' and could be the basis of further discussions on which entities should be included as potential receiving schemes as part of an automatic small pots transfer eco-system. The list is not intended to exclude other entities from being part of a small pots solution, however, it is likely that further due diligence checks would need to be carried out before a transfer could be made to any schemes not on the list.

COMPULSION

The Group is agreed that legislative changes would be required to enable the transfer of small pots without consent from contract-based schemes, subject to a future positive finding of a cost/ benefit analysis. The aim would be to ensure that there is a level playing field between contract and trust-based automatic enrolment schemes. As a minimum, the industry representatives noted that the legislative framework would need to authorise trustees and providers of such schemes to transfer a small pot without consent notwithstanding anything contrary to this in the scheme rules and/or the contract between the provider and relevant savers. In the view of pensions industry representatives on the group, in order to implement an efficient transfer solution it would also be necessary for the legislative changes to compel schemes and providers to transfer any small pots that are in scope.

The introduction of a compulsory regime would also facilitate the transfer of small pots from authorised master trusts and other trust-based schemes and support the establishment of an automated transfer process (where appropriate).

NEXT STEPS AND INITIAL CONCLUSIONS

We have split the regulatory and legislative recommendations into those relating to the current transfer process and those relating to a future automatic transfer process below.

	AREA	RESPONSIBILITY	LATEST EXPECTED COMPLETION
Recommendations for current transfer processes	Update guidance to require trustees or scheme providers to keep personal contact details (including email) as already prescribed in the legislation. Expanding common data requirements to include holding saver mobile phone numbers might also be helpful	TPR	2022
	Request for TPR guidance to support transfers between charge capped default funds within authorised master trusts	TPR	Ongoing
Recommendations for any future automatic transfer process	Consideration of the feasibility of a low-cost, at-scale transfer process for small pot consolidation initially between master trusts, and potentially with wider application	Sub-Group of Master Trust	Ongoing, reporting in 2021
	Other studies or pilots to consider the feasibility of a low-cost at-scale transfer process for small pots as appropriate	Industry	Ongoing
	Consideration of small pots carve out or other solutions in upcoming regulatory initiatives (see Chapter 8)	DWP, HMT, FCA	Ongoing
	Identifying preferred consolidation model(s) and key elements of legislative and regulatory framework	Co-ordination group, DWP, TPR and FCA	Ongoing
	Consideration of exemptions from certain regulatory requirements for small pots i.e. COBS 13.1 and SMPI (Disclosure Regs 2013)	DWP, FCA	2023

	AREA	RESPONSIBILITY	LATEST EXPECTED COMPLETION
	Encouraging digital communication, making sure pension communications can be effectively sent and received by email and SMS i.e. by including email as a required item within automatic enrolment jobholder information	DWP, FCA, TPR	2023
	Agreed definition of a deferred member in the small pot context in legislation e.g. pots which have not received contributions for a predetermined amount of time	DWP with TPR involvement	2023
	Automatic transfer opt-out embedded in existing customer communications e.g. new scheme documents	DWP	2023

FURTHER EVIDENTIAL NEEDS

Further research that would help inform this work:

- Research needs to be carried out into the effect of moving an estimated 2.5 million pots and if there would be an issue with so many small pots being divested from funds, assuming in a short space of time. Following the initial glut of transfers this should decrease to a natural flow where people are simply moving jobs.
- Further research on the feasibility of a low-cost, at-scale transfer process to be produced by a sub-group of master trust schemes in 2021.
- Further detailed research may be needed looking at each of the recommendations outlined in the process mapping to see, where possible, what value each of these asks saves and what proportion of small pots would be lost with each step in the transfer process.
- Understanding saver preferences by updating consumer research previously carried out to understand where savers would want their money automatically transferred to out of the automatic transfer destinations: to follow them to their new employer scheme, or to a central aggregator [39].

39 ABI Consumer research - 2012

CHAPTER 6: PENSIONS DASHBOARDS

SUMMARY

- Previous work on small pots has identified that Pensions Dashboards may be supportive of resolving the proliferation of lost pots, and that exploring leveraging learnings from matching and data standards under development may be efficient.
- The Co-ordination Group has identified and analysed common elements between the future potential small pots solutions (in so far as they are currently understood) and Dashboards, and illuminated the barriers for reuse.
- The initial administrative assessment demonstrates the need for more work to fully uncover the potential alignment between the two initiatives.

As the DWP Chaired Small Pots Working Group in 2020 noted, Pensions Dashboards may form part of the small pots solution in so far as they help savers and small pots consolidation by enabling individuals to access their pensions information online, securely and all in one place. However, it also noted that by itself Pensions Dashboards would not reverse the trend in growth of small deferred pots or remove the totality of costs in the system. Pensions Dashboards was therefore found to be one element of a wider small pots solution.

Additionally, one of the conclusions of the previous DWP Chaired Small Pots Working Group was for Dashboards to provide a starting point to build-out from for the purposes of underpinning future large-scale deferred small pot consolidation and that learnings from Dashboards should be maximised. Further work is still needed to consider whether the approaches adopted for that developed for Dashboards infrastructure and architecture could be helpful in a small pots context, and initial conclusions are reflected below. The systems and timelines envisaged for small pots solutions and Pensions Dashboards remain separate.

DASHBOARDS 'FINDER' INFRASTRUCTURE AND ARCHITECTURE

There are a number of elements of similarities and differences between Dashboards and Small Pots solutions, and necessary data standards. We believe that if a small pots architecture is built in the future, there are elements which could be reused from Dashboards (i.e. matching criteria). These elements have been identified in the table below.

ELEMENT OF THE SOLUTION	DASHBOARDS	SMALL POTS CONSOLIDATION
High level architecture	Defined in DWP April 2019 consultation response and based on user-managed consents in line with the Data Protection Act 2018 (UK GDPR).	Default consolidator and automatic pot follows member both still under consideration but would require a different architectural design than is being used for dashboards in order to support an automated approach. Results from PPI Data Project may help choose which approach to take, maybe in 2022. The Co-ordination Group will further consider the models.
Process flow assumptions	Flows for individual (i.e. dashboard user) driven Find process, and scheme response View process, both well developed and understood.	Assumption of cyclical "pull" process by participating schemes under some models – not yet confirmed.

ELEMENT OF THE SOLUTION	DASHBOARDS	SMALL POTS CONSOLIDATION
Overarching legislation	Primary in place, draft secondary expected for consultation in Dec 2021.	Highly likely to be needed to give trustees legislative "cover" and to regulate a small pots eco-system.
Schemes in scope	All	Assumption automatic enrolment DC schemes.
Pensions in scope	Pensions in payment and crystallised benefits are not in scope.	"Small pots" –current working assumptions are up to £500. See Chapter 3.
Central Identity service	Interim Procurement starts Oct 2021, ends Dec 2021. Temporary solution.	Potential to reuse Dashboards IDS, with adaptations, although Dashboards' long term solution is the DCMS digital identity and trust framework (not yet in place).
Central Consent and Authorisation Service	Procurement of supplier concludes Sep 2021, alpha service by end of 2021.	Not yet clear whether required as part of the automatic small pots consolidation ecosystem.
Pension Finder Service	Procurement of supplier concluded Sep 2021 [40], alpha service by end of 2021.	Initial conversations have suggested that the Pension Finder Service would not be able to be adapted for a small pots solution.
Governance Register	Procurement of supplier concludes Sep 2021, alpha service by end of 2021.	Potential to reuse Dashboards GR, with adaptations.
ISP connections to the ecosystem	Alpha data providers connecting from late 2021.	Potential to reuse of elements of the Dashboards connections, but with different APIs.
Data provision solutions	ISPs and other data providers will, by whatever means, provide and maintain a standardised "data layer" that will be exposed to the pensions dashboards find and view services. This will include estimated retirement income and accrued pension data, as set out in the PDP Data Standards and subject to the final agreed approach is in this area.	Potential to re-use this data layer with probably minimal additions to support small pots consolidation. Subject to regulations.

40 https://www.pensionsdashboardsprogramme.org.uk/2021/09/06/pdp-appoints-capgemini-supply-digital-architecture/

Industry data matching conventions (DMCs)	Plan for initial version of DMCs by end of 2021, to be further enhanced through beta testing during 2022. For partial matches, where a pension scheme / provider makes such a partial match with the 'Find' data (from a dashboard find request), manual processes will need to be developed to enable the individual to get in touch with the scheme / provider directly. If the individual does get in touch, there will be an opportunity for their data held by the scheme / provider to be updated, via existing data maintenance processes.	Potential to reuse data matching conventions, with adaptations due to the difference in engagement in the consumers likely to have small pots i.e. they cannot be relied on to 'self verification' of partial matches. There is probably a much higher likelihood of persuading members to engage with a dashboard driven process (of verifying/updating their data) than there would be for auto-transfers. This is a key process difference.
Transfer Service	Not applicable.	New technology component potentially required.
Ecosystem regulation	Dashboards regulation regime under development.	Small pots consolidation regulation likely to be required.

BARRIERS TO USING DASHBOARDS INFRASTRUCTURE

As identified in the table above, there may be legislative barriers to using Pensions Dashboards infrastructure for Small Pots. Further investigatory work is needed to determine if the infrastructure suitable to use and, if so, if it is able to do so.

The Pensions Dashboards structures have not been developed with small pots in mind. There are differences in how they would be used, and they would require some adaptations or additions to the "Dashboards versions" of the different ecosystem components. However, small pots considerations should not slow down the progress of the development of the pensions dashboards eco-system. For example, in the future, conversations may be needed with the vendor[41] of the pensions finder service to discuss ways of building on this knowledge and innovation. However, this is not likely to be an immediate conversation. It will also be important to explore other technical solutions and the working group will keep an open mind about this.

The Group has considered whether it would be feasible for the Pension Finder Service to be suitable in a small pots for consolidation using similar APIs. However, the high level architectural design for dashboards does not support automated consolidation so it is likely that a finder service to enable this would need to form part of a separate eco-system with its own regulatory framework. Also, additional validations will be required such as determining if the pot that has been found matches the small pots criteria and what controls are in place to ensure an organisation has the authority to request to consolidate a small pot in a "pull" scenario.

We believe however that there is an important distinction to be drawn here between the "central" components of the dashboards eco-system being procured by the PDP, and the wider development being carried out by industry, particularly around data provision and capabilities of ISPs. This wider development is in its infancy, so the industry should be encouraged now to take account of the likely future re-purposing of this data standardisation and how such interoperability can support a future Small Pots consolidation infrastructure. Further consideration around the framework of ISPs and regulations will be needed.

41 In September the Pensions Dashboards Programme announced that Capgemini, in partnership with Origo, will deliver specific elements of the central digital architecture, including the pensions finder services, consent and authorisation service and governance register.

From a pure data provision perspective dashboards and small pots challenges appear very similar, and having "an eye" on small pots requirements would be unlikely to create any material delay in the timescales for industry development in support of pensions dashboards.

NEXT STEPS AND INITIAL CONCLUSIONS

We believe that the following are likely to benefit savers with small pots:

- Conversations are planned between the Small Pots Co-ordination Group and the Pensions Dashboards programme to explore opportunities and challenges in closer alignment; particularly learnings from data matching and data standards.
- Further activity is needed to explore alternative technical solutions.
- We recommend focusing resources on getting the Pensions Dashboards core ecosystem set up and running, rather than diverting attention to Small Pots requirements, but with the caveat that the successful vendor should be kept abreast of developments on Small Pots so that this can be taken account of in decision making, but without delaying the pensions dashboards ecosystem development timeframes. Additionally, other vendors may be more suited to delivering small pots solutions.

CHAPTER 7: MEMBER EXCHANGE PILOT

SUMMARY

- In parallel the four largest master trusts by membership have been exploring the potential for a small-scale proof of concept pilot of Member Exchange, a potential short term solution to the small pots problem.
- The work so far has identified that legal advice, a trusted third party and trustee comfort are all crucial to progress the pilot, and efforts continue on these areas.

WHAT IS MEMBER EXCHANGE?

Member Exchange is a potential concept that has been created in the search for ways in which the industry can ameliorate the spread of small deferred pension pots before Government introduces legislation to provide a full solution to the small pot issue.

It is referred to as a "potential concept" because it is un-tried and un-tested and the hypothesis that it can be done under the cover of existing legislation may yet be found wanting.

A Member Exchange is done between two master trusts, and involves members who have a small deferred pot at one master trust and an active pot at another master trust being identified and then having their deferred pot transferred onto their active pot.

Industry recognises that the auto-enrolment practice of joining by inertia has often led to low levels of member engagement. And that low engagement is particularly prevalent amongst those with small deferred pots. So whilst the members identified for transfer in the Member Exchange will be sent notification that this is the course of action their trustee proposes along with instructions on how to opt-out of the process, if no response is received the transfer will be completed without member consent.

Each Member Exchange is a bilateral swap between two master trusts. However, a wider exchange can be achieved by organising a simultaneous series of such bilateral exchanges involving more than two master trusts.

The key legislative power that is being relied on is the Occupational Pension Schemes (Preservation of Benefit) Regulations 1991, which give trustees the discretion to undertake a bulk transfer of members without consent. DWP have published extensive guidance to trustees [42] and law firm Squire Patton Boggs have published a two-page summary of the same guidance [43].

UPDATE ON PROGRESS

In response to the call by the DWP chaired Industry Small Pots Working Group that consideration should be given to conducting a Pilot Member Exchange, the policy heads of the four largest master trusts by member numbers have, in parallel with the work being done by the Small Pots Industry Co-ordination Group, been investigating the potential for a small scale pilot using actual live cases.

The purpose of using live cases is so that a pilot can, after the transfer has taken place, include a member survey to establish members' reactions to having their pensions identified and transferred in this way. Early in the process it became apparent that the Constitution of NEST does not contain a trustee power to transfer members out without their consent. Accordingly NEST became simply an observer to the process, leaving the three master trusts NOW: Pensions, The People's Pension and Smart Pension as potential candidates for a Pilot Member Exchange.

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42 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/722295/occupational-pensions-bulk-transfers-without-consent-guidance.pdf

43 https://www.squirepattonboggs.com/-/media/files/insights/publications/2018/09/how2-do-pensions-bulk-transfers-without-consent-defined-contribution-benefits/bulk-transfers-without-consent-defined-contribution-benefits.pdf

In September a workshop was held for the Trustee Chairs of the three master trusts. Policy Heads organised the agenda papers and facilitated the workshop. The workshop was attended by a leading pensions lawyer, contributing in an informal capacity, and also by NEST's Policy Head as an observer.

The workshop examined the benefits of Member Exchange, looked at certain details of how a pilot might operate and brainstormed the areas that will need consideration before trustee discretion can be exercised. In the concluding stage of the workshop, the three Trustee Chairs expressed cautious guarded optimism whilst noting that there are still several major hurdles to overcome and that this will require both cost to the Scheme Funder and time and resource from trustees and administrators.

FINDINGS SO FAR

1. Legal advice is required on the position under Competition Law of two master trusts conducting a Member Exchange together. And with particular reference to the Pilot Member Exchange, legal advice is required on the position of a closed group of three master trusts organising a pilot amongst just themselves without access by the wider master trust community.
2. Legal advice is required on what are major Data Protection implications. Each master trust will need expert guidance on whether their Privacy Statement grants them scope to share personal member data in the way proposed and whether it has been adequately drawn to the members' attention.
3. There will be a crucial role for a Trusted Third Party (T3P) to receive data from each master trust, to identify matches, and to return to each trustee details of which members are to be transferred to the other master trust. The selection of the T3P will be a complex process. It will need to be a joint procurement by all three master trusts. It will need due diligence of the T3P to provide satisfaction that it has the required competencies to handle the data, maintain confidentiality, avoid data corruption and to make the correct matches. It will need appropriate assurances from the T3P.
4. Once all of the above is in place, it is still not a simple decision for a Trustee Board to authorise a Pilot Member Exchange. The Regulations together with wider fiduciary responsibilities place a heavy duty on trustees to undertake a thorough decision making process, considering all relevant factors and discarding any irrelevant factors to ensure that the Member Exchange furthers the purpose of the trust and is generally in the interests of its members taken as a whole.

NEXT STEPS

- Policy Heads in each participating master trust to investigate practicality of appointing one law firm to provide overarching legal advice on the Competition Law, Data Protection and Fiduciary Duty aspects to all four master trusts involved in the pilot.
- Policy Heads in each participating master trust to begin compiling a list of the skills and attributes required by the Trusted Third Party that will be needed for the data sharing
- TPR and DWP to be updated on the emerging findings from the Trustee Workshop and subsequent investigations.

CHAPTER 8: OTHER GOVERNMENT AND REGULATORY INITIATIVES

SUMMARY

- The Co-ordination Group has identified other Government and regulatory initiatives, which may impact on the degree to which it is possible to (automatically) consolidate small pots now and in the future.
- Further analysis should be undertaken to ensure that barriers to small pot consolidation are removed, and that initiatives supportive of automatic consolidation are pursued.

There are a number of legislative/regulatory matters that would benefit from further more detailed consideration by the Co-ordination Group to better understand and assess the potential impacts in relation to small pot consolidation solutions. The Co-ordination Group expect to carry out further work on this, in order to try and assess these impacts more precisely, including building the evidence base on the scale/ nature of these issues in respect of small pots in the AE workplace pensions market that come within scope of the working assumptions in this report:

- ***Pension transfers and scams 'red flags'***
  Though this intervention is designed to protect members from scams, industry representatives noted it does place an additional burden on schemes where they must undertake additional tests against the conditions for transfers, and members where they must provide evidence of employment where the transfer isn't to a scheme identified as a low-risk scheme.
- ***Same scheme consolidation***
  It was a recommendation in the small pots working group report for Providers to make progress on consolidating multiple pots within charge-capped default funds for the same deferred members should consolidate those pots over the next 3-4 years. Where it is possible, providers have been making progress on this. Same scheme consolidation is unlikely to occur for contract-based schemes, given the need for member consent to consolidate their benefits even within the same scheme or between schemes run by the same provider. Further analysis is needed to understand how far same scheme consolidation goes to resolve part of the small pots challenge. The Group will work with DWP to monitor progress on this.
- ***The £100 de minimis***
  Some of the industry representatives on the Group noted that the introduction of the de minimis also complicates small pots consolidation at the lower end of the scale. Further consideration is needed to consider circumstances in which it will be appropriate to consolidate a pot which is not subject to a flat fee because it is worth £100 or less where a flat fee will be applied to the consolidated savings under the receiving scheme.
- ***Protected pension ages***
  Where a small pot benefits from a protected pension age (either under the current protected pension age regime or the regime which the government is planning to introduce when the normal minimum pension age increases to age 57 in April 2028) industry representatives noted that a saver would lose the benefit of that protection if their pot is transferred into a pot which does not benefit from a protected pension age, unless the transfer benefits from the protection afforded on block transfers or the proposed protection on individual transfers (which will apply under the April 2028 protection regime).

  However, if savers were permitted to retain their protected pension age following a small pot transfer this could create additional administrative difficulties for schemes and providers if they are required to ring-fence the transferred in benefits as proposed under the April 2028 protection regime. A transfer may not be in the saver's interests if they cannot accrue benefits in the transferred, protected pot in the new scheme. This is because the amount they can access at 55 will be limited by ring-fencing it.

In addition, savers with a small pot that benefits from a protected pension age would also have the option of transferring savings from other schemes which do not benefit from a protected pension age into the fund which benefits from the protected pension age in order to access those funds earlier. This option would be lost if a small pot which benefits from a protected pension age is transferred into a pot that does not benefit from this for any amount that is not ring-fenced, and the saver does not have any other arrangements which benefit from a protected pension age. In addition, ring-fencing would prevent within-scheme consolidation and any benefits for the customer of that approach will not apply.

- ***Stronger nudge***
  Under the Stronger Nudge proposed approaches (both DWP and FCA), all pots will end up being nudged to guidance, regardless of size. In line with the requirements of the Financial Guidance and Claims Act 2018, the DWP and FCA have proposed those who are transferring for the purpose of accessing their pension savings should be nudged to Pension Wise. Industry representatives noted that this could add another layer of cost to every pot as someone needs do the nudge and undertake a check to ensure that the nudge has happened.
- ***Future of DC Consolidation***
  It is important to note that the pensions industry representatives on the Group thought that consolidation of schemes will not necessarily result in pot consolidation. In many cases administration for different employers remain separate even after transfer to a consolidator scheme. Moreover, where pots have guarantees or special characteristics they may not be able to be consolidated (without losing these highly valuable benefits for the member) with other pots even in a 'consolidated' scheme. However, having an eventual smaller number of DC schemes may make it easier to implement an industry solution for small pots where this relies on bulk transfers of significant scale to reduce the per-transfer cost. Though the solution would need to be in place before any significant consolidation were to occur to realise this eventual scale benefit.
- ***FCA/TPR Customer Journey, DWP Statement Seasons, DWP Simpler Annual Benefit Statements and other communications and engagement initiatives***
  Small pots can undermine the engagement experience and consumer journey, and other initiatives should be considered with savers experience of small pots in mind.
- ***Open finance***
  Similar to work ongoing on Dashboards open finance initiatives will, in some parts of the workplace pensions industry, positively impact on the manner in which members will be able to engage with their small pots. In March 2021 FCA published their feedback statement on a Call for Input in open finance.
- ***LTAFs and Illiquids***
  Transfer times for small pots may be impacted by increased holding in illiquid funds with infrequent redemption dates or increase change of gating. Work is ongoing to consider whether re-registration and in specie transfers could form part of the new proposed structures, and this will impact on the degree to which low-cost transfers are possible.
- ***FCA Consumer Duty***
  The FCA has consulted on a new consumer Duty to raise standards generally in financial services. The FCA's stated aim is to ensure that firms adequately consider the needs of their customers and prioritise good consumer outcomes as an objective of their business activities. The FCA aims to publish a second consultation paper later in 2021, which may be relevant for firms dealing with small pots.

LEGISLATIVE/REGULATORY CONSIDERATIONS

- Clarity is needed on potential policy changes and how this would affect automatic transfers.
  For example:
  - Change to pensions tax
  - Pensions dashboard implementation
  - FCA/TPR customer journey
  - Statement season

CHAPTER 9: NEXT STEPS

The current prioritised models (pot follows member, default consolidators and member exchange) have different administration challenges and that has limited how much progress some of the groups have been able to make in some areas. A decision on this fundamental point needs to be made sooner rather than later so that all stakeholders have clarity about this.

There are a number of outstanding areas of work, which need to be completed in the next phase of the work. The priority being:

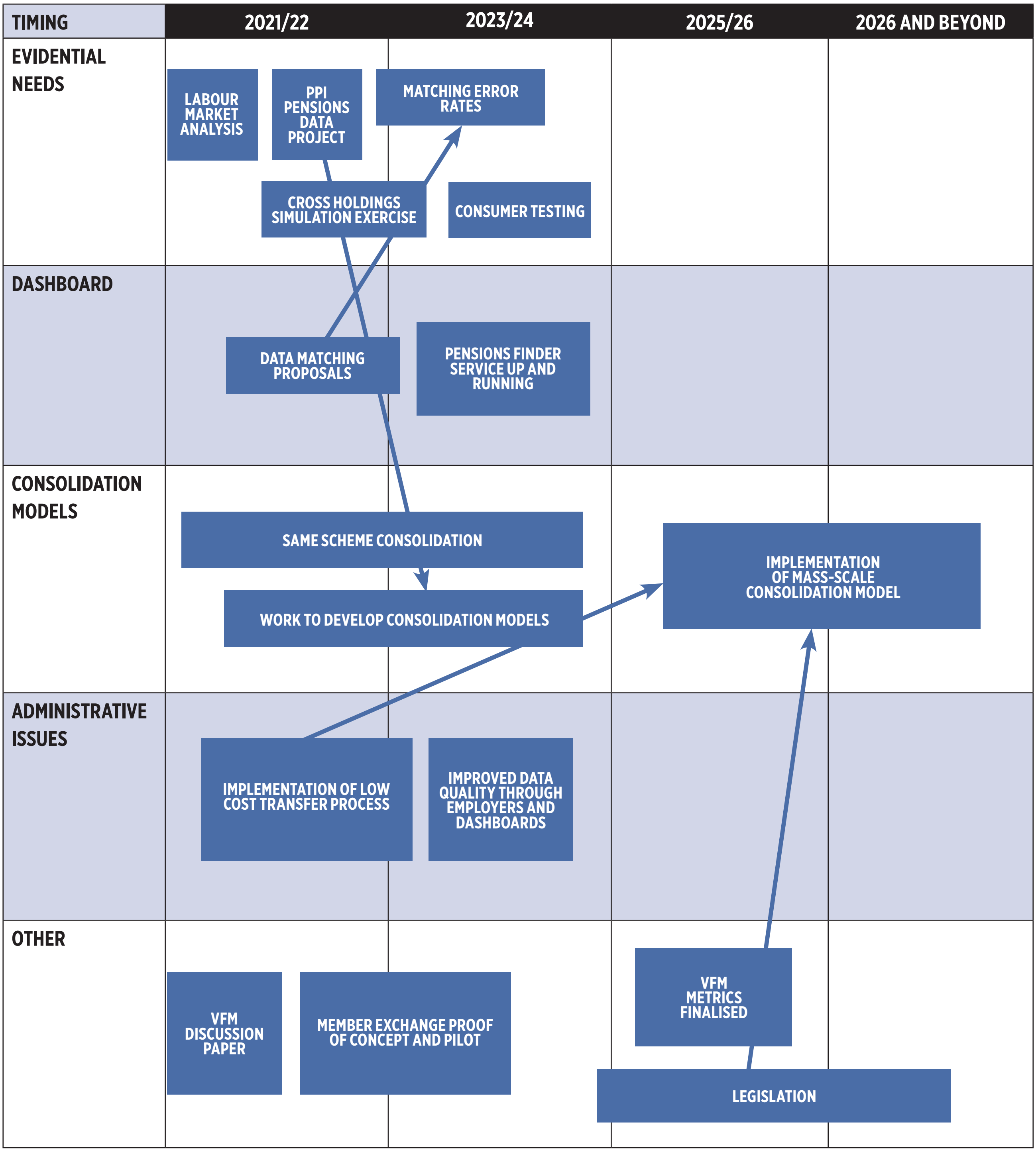
- Consideration of Pensions Act 2014 pot follows member legislation and what could be achieved through using this and new secondary legislation. The legislation needs to be reviewed to understand whether default consolidators, as well as pot follows member, could fit within the existing legislation.
- Literature review of current evidence of benefit of small pot consolidation.
- An analysis of the "system" efficiency benefits of eliminating the cost of administering small pots, with credible assumptions about the flow of these benefits to schemes and members
- Progress work on identifying the optimum small pots models:
  - Assess the models against newly refined principles based on those developed by the DWP chaired working group, particularly considering whether 'stock' and 'flow' small pots issues require different solutions.
  - Reviewing how potential consumer detriment might vary depending on the model being considered; the nature and scale of detriment that consumers face may be different depending on which model is chosen. This needs to be considered in more detail when evaluating the remaining models still under consideration.
  - The process flows (both "push" and "pull" in a small pots eco-system: More work is needed to understand what a small pots eco-system would look like and the resulting process flows. Once this has been developed, work on data standards could progress.
  - Impact analysis is needed to understand the movement of small pots under different models and the impact on the market (see evidential needs). This analysis should be comprehensive and, for example, assess whether the movement of pots under pot follows member or a default consolidator model differ and the impact this has on the financial sustainability of the whole automatic enrolment system. A solution will need to benefit those being auto-transferred and bolster the financial sustainability of the automatic enrolment world, and maintain choice for employers.

Other work that is progressing but with a longer time line are:

- Continuing to make progress on same scheme consolidation where possible. The Roadmap in the small pots working group report gave a timeline until 2023/24 for schemes to prepare for this consolidation. Schemes have been making progress on this although it is still an issue for schemes. DWP are undertaking a data collection exercise to understand what progress has been made in this area.
- Continuing with the exploration of a member exchange pilot.
- Continuing consideration of legal issues. As noted in several parts of this report, further work will be required to ensure that any legal risks for trustees, providers and/or members associated with changes to implement a consolidation model are understood and addressed as part of this project. Legal issues that the Co-ordination Group are currently considering include, but are not limited to, appropriate statutory protection and easements for transferring trustees/providers and avoiding the loss of any member tax protections as a result of an automatic, without-consent, transfer, e.g. protected pension ages and protected cash lump sums pursuant to the Finance Act 2004.

CO-ORDINATION GROUP ROADMAP

The below roadmap illustrates the Co-ordination Groups' reflections on the optimum delivery time for outputs of certain elements of the next phases of the development of a small pots solution, and plots these on a rough timeline.



FURTHER EVIDENTIAL NEEDS

A number of evidential needs, to support decisions around what a future longer-term consolidation model and to build an evidence base for change, have been identified by the Group. In the next phase the Group will work with DWP to confirm the asks, priorities and timescales.

The Group believes these evidential needs will help form the pathway to implementation of a whole of market small pots solution for both trust and contract based schemes.

AREA		RESPONSIBILITY
Reasons for Pot creation	We need to understand the reasons small pots are created. Employer vs scheme vs member issues. (We looked briefly at potential issues with the a-e/opt out process in the DWP group, but this needs more work – we ought to prevent the creation of small pots where we can)	DWP best placed to undertake
	Labour market analysis to understand the creation of small pots in more detail	DWP best placed to undertake
Benefit of small pot consolidation	Literature exploring benefits of small pot consolidation and identifying missing areas where research is needed	Industry
The analytical next steps identified in the Small Pots Working Group report in December 2020	Evaluation of costs and benefits and proof of value for money, modelling impacts on individuals in different circumstances	*In each case, DWP best placed with industry input*
	More comprehensive evidence on the average size of deferred pots and how many are being generated (and how many are already transferred)	
	Further economic/market impact analysis in relation to the consolidator model	
	Research needs to be carried out into the effect of moving an estimated 2.5 million pots and if there would be an issue with so many small pots being divested from funds, assuming in a short space of time. Following the initial glut of transfers this should decrease to a natural flow where people are simply moving jobs	
	Consumer Journey research	

Pensions Data Project	The spread of small pots across the market both by member and provider (e.g. the degree to which non-UK nationals being automatically enrolled as a result of short periods of seasonal work result in a problem for some master trusts)	*PPI*
	Simulation exercises to understand cross-holdings and costs of matching and transferring pots en masse	Future work may need volunteers supported by Co-ordination Group, regulators and DWP
Evidence from other countries (building on previous PPI report)	Review small pots process flows in other countries, for example, Australia Literature review of evidence on benefit of small pot consolidation and new research if required to evidence the intrinsic benefits to members of pot consolidation	Industry
	More detail on other countries' experience on how their respective systems are set up e.g. liability models	Industry
Saver preferences	Updating consumer research previously carried out to understand where savers would want their money automatically transferred to out of the automatic transfer destinations: to follow them to their new employer scheme, or to a central aggregator [44]	DWP
Error rates of matching	Matching, and understanding the likely error rates of different options, and deciding acceptable practices/procedures where an error occurs	Part of dashboard work
	The life journey of NINo and where errors are arising	DWP and Industry

SUMMARY OF INITIAL CO-ORDINATION GROUP CONCLUSIONS

Adjustments to these recommendations and additional conclusions are expected and will be included in the next report of the Co-ordination group which will reflect all the work undertaken in 2021.

44 ABI Consumer research - 2012

We believe that the following are likely to benefit savers with small pots:

Administrative issues

- Further understanding of the reliability of matches using existing data criteria and understanding how far a unique identifier can overcome some of the inefficiencies with existing data.
- Providers work with employers and government to improve data quality, where they are able to, for example, government could help to verify data held by schemes. Particular focus should be placed on the need to provide sufficient data for effective member matching as part of employee set up.
- Update guidance to require trustees or scheme providers to keep personal contact details (including email) as already prescribed in the legislation. Expanding common data requirements to include holding saver mobile phone numbers might also be helpful.
- Consideration of the feasibility of a low-cost, at-scale transfer process for small pot consolidation initially between master trusts, and potentially with wider application. Other studies or pilots potentially to be set up, as appropriate.
- Conversations are planned between the Small Pots Co-ordination Group and the Pensions Dashboards programme to explore opportunities and challenges in closer alignment; particularly learnings from data matching and data standards.
- Small pots data matching protocols align with those for Pensions Dashboards and should be considered as part of the ongoing work by PASA, PLSA and ABI on Pensions Dashboards Data Matching Conventions (DMCs), whilst recognising that the different context of small pots consolidation may require stricter criteria.
- Ensure that the current phase of industry development supporting Pensions Dashboards,, such as the design and build of ISP services, is informed and aware of the future matching requirements of Small Pots.
- We recommend focusing resources on getting the Pensions Dashboards core eco-system set up and running, rather than diverting attention to Small Pots requirements, but with the caveat that the successful vendor should be kept abreast of developments on Small Pots so that this can be taken account of in decision making, but without delaying the pensions dashboards ecosystem development timeframes. Additionally, other vendors may be more suited to delivering a small pots solutions.

Overall, the project needs to be guided by the delivery of member benefits and the management and mitigation of risks to member interests. The first step here is a substantial impact assessment to evidence and quantify the benefits to members of the systemic efficiency improvements and cost reductions and the benefits to individuals of consolidation. The clear establishment of these benefits will guide other key decisions:

- the confidence of trustees that automatic consolidation transfers are, in the round, beneficial to members,
- the government's decision on whether to legislate,
- the staging and pace of progress of bringing more categories of small pots into scope.

Factors of assessment of future consolidation models

- Identifying preferred consolidation model(s) and key elements of legislative and regulatory framework.
- Further consideration of the conditions for transferring small pots under an automatic small pots solution and the balance of potential detriment and benefits to savers, and delivering a low-cost process.
- Review and agree assumptions for a small pots ecosystem and develop high-level process maps for both "push" and "pull" models.
- Once further model design work is undertaken, the pots in scope should be modelled against them to assess the impact on savers and the Automatic Enrolment market.
- Request for TPR guidance to support transfers between charge capped default funds within authorised master trusts.

Implementation of future consolidation models

- Pots within scope of future automatic transfers should be:
  - Small deferred pots within default funds and Sharia funds under qualifying schemes.
  - A suitable trigger for identifying a deferred pot and when it can be transferred need to be considered against the different consolidation models and as part of the consumer journey research and labour market analysis.
- Agreed definition of a deferred member in the small pot context in legislation.
- Automatic transfer opt-out embedded in existing customer communications e.g. new scheme documents.
- Exemptions for small pots automatic transfer process from existing requirements, i.e. COBS 13.1 and SMPI (Disclosure Regs 2013).
- Consideration of small pots carve out or other solutions in upcoming regulatory initiatives.
- Encouraging digital communication, making sure pension communications can be effectively sent and received by email and SMS i.e. by including email as a required item within automatic enrolment jobholder information.
- Implementation of a small pots solution should be staged, starting with what is possible within the current confines of existing legislation.

FUTURE LEGISLATIVE/REGULATORY CONSIDERATIONS

As noted throughout this initial report of the Co-ordination Group there are many ways in which the current legislative framework presents barriers to automatic small pot consolidation in the workplace pensions market or could more clearly support any future solutions.

- To facilitate automatic transfers in contract-based schemes (Group Personal Pension), there would have to be a legislative override (as outlined in Chapter 5).
- In the long-term, the Group considers that it will be necessary for the government to legislate to compel trust-based schemes and authorised managers of contract bases schemes to transfer and accept small deferred pots in order to properly address the issue of small pots (as outlined in Chapter 1).
- Consideration of how any small pots transfer model would interact with upcoming legislative and regulatory initiatives (for example, stronger nudge, increase in the normal minimum pension age, a de minimus for flat fees and new transfer conditions) (as outlined in Chapter 8).
- For the automatic transfer of agreed small pots to be exempt from certain regulatory and legislative requirements. For instance, pre-sale illustration requirements – COBS 13.1 and SMPI (as outlined in Chapter 5).
- In advance of any legislative compulsory transfer framework, it could be helpful to have assurance or a statement from the Regulator to facilitate small pots transfers.
  - As we are exploring the opportunity for transferring and consolidating small deferred pots in the automatic enrolment market, and as currently we believe the balance of small deferred pots reside in automatic enrolment master trusts, the Member Exchange pilot (Chapter 7) will inform the extent to which transferring and consolidating small deferred pots is feasible within existing legislation and current trustee comfort.
  - It is possible that the pilot, or other work, will identify the degree to which helpful assurance could be provided by the Pensions Regulator to deliver additional comfort for trustees and relevant parties to facilitate small deferred pot transfers.
  - Any such assurance from the Regulator should therefore be intended to help give some comfort to trustees in the short and medium term and could help unlock solutions that could work for ‘stock’ pots. The Regulator may, for example, be able to provide a statement highlighting the holistic approach trustees must take, including the benefit to members of having fewer small, deferred pots.
  - This is notwithstanding that the statement will be unlikely to establish rights savers have in the case of transfers they are not happy with (Chapter 4) or assert which schemes offer relative value for money. Particularly, some reassurance could be provided by Regulators and Government that new scams and other legislation should not be a barrier to transfers to Master Trusts (Chapter 8).

The Group will continue to consider the need for supportive contributions in the next stage of the work.

ANNEX 1: SUMMARY OF RECOMMENDATIONS AND ROADMAP FROM THE SMALL PENSION POTS WORKING GROUP REPORT, DECEMBER 2020

SUMMARY OF RECOMMENDATIONS

The small pots working group identified the following conclusions, recommendations and actions for the pensions industry and government to work together to develop effective solutions, with the aim of delivering better value for scheme members. We are calling on the pensions industry including pension providers, their representatives and delivery agents, working jointly with government and regulators, to take forward these recommendations over the medium term:

- the pensions industry, government and regulators should continue to explore and enable opportunities for member-initiated consolidation, with proportionate member safeguards, particularly in respect of deferred, small pots above a certain value. This can complement other interventions that will be necessary for deferred low value pension pots. Technology and tools, such as pensions dashboards that allow members to view all pots with different providers in one place, could facilitate more consolidation in the future
- member-led consolidation alone, however, is unlikely to change the trend in the growth of defined contribution (DC) deferred, small pots. The pensions industry, working jointly with government, should prioritise action on enabling automatic and automated large-scale low- cost transfers and consolidation for the automatic enrolment mass-market. Member safeguards should provide proportionate protection, but not act as a barrier
- where pension providers are holding multiple pots within charge-capped default funds for the same deferred members, the direction should be to consolidate those pots. Recognising, however, that it is not always possible or desirable (for example because of member consent associated with scheme terms and conditions), we recommend pension providers should in the interim work towards implementing a single consumer facing view (within a single member portal, with information on their pension pots). It could be achieved, following scoping work in 2021 and 2022, through adoption of industry best practice and regulatory guidance
- the pensions industry should establish operational focussed groups, to investigate and address administrative challenges which will be necessary to underpin mass transfer and consolidation systems that can be delivered at scale within the automatic enrolment market. Consideration will need to be given to the appropriate governance structure to ensure effective transparency and reporting arrangements. The groups should focus on the following areas, with the aim of making available an initial publicised update in summer 2021

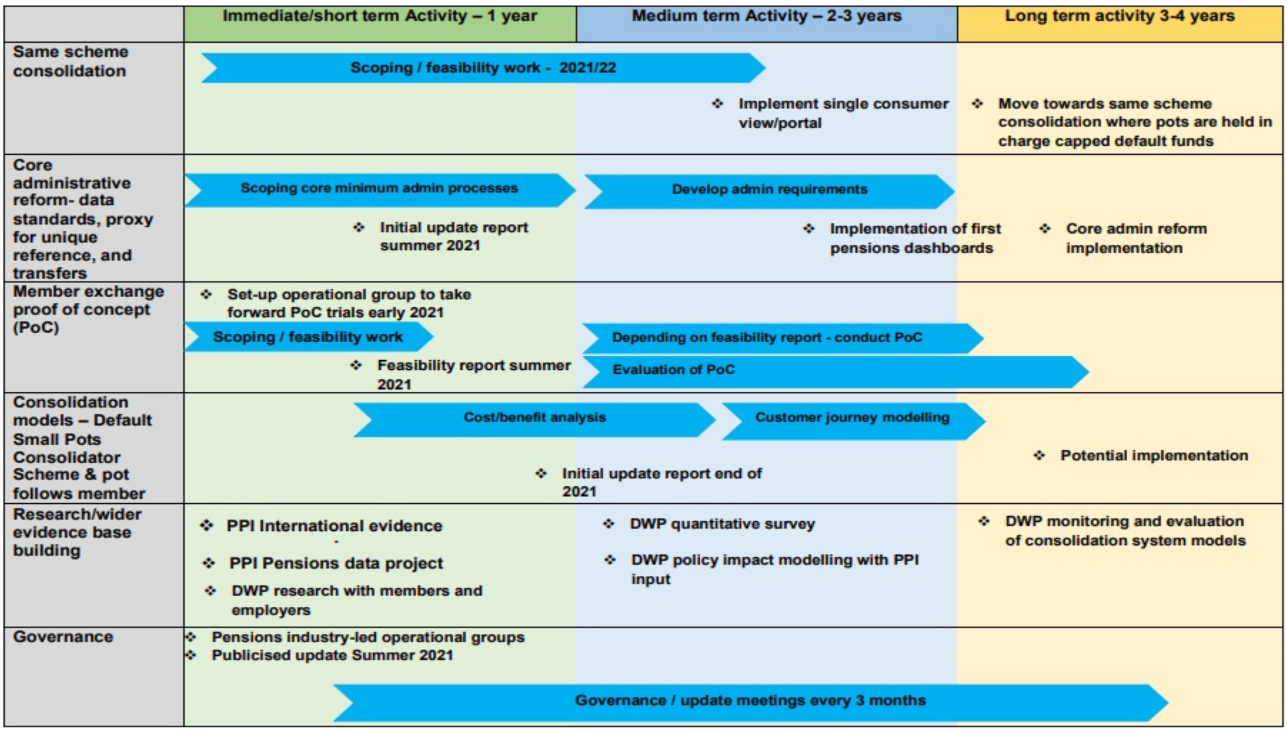
a) Activity should be prioritised on scoping the core minimum viable administrative processes, including:

- developing and testing data that would provide sufficient matching capability, compliant with data sharing legislation, (as a proxy for a unique reference) to verify the identity of the person whose pot(s) will be transferred is the same as the identity of the person whose pot will receive the transfer. Opportunities to build out from data-matching in relation to pensions dashboards; the PPI's work on the Pensions Data Project and industry good practice should be maximised
- developing and adoption of common standards is a key underlying element to support effective consolidation. The pensions dashboards data standards[footnote 6] would provide a starting point to build out from, which could then be tested by providers ahead of confirming standards which could be codified by the industry
- identifying requirements for a low-cost bulk transfer process. This should start with an end to end review of the current individual transfer process to identify where cost occurs in the system and where friction can be removed – however mass transfers which are non-member led may necessitate new approaches to achieve low-cost delivery, while maintaining proportionate safeguards for members

b) Member-exchange proof of concept trials involving low value small pots within master trust schemes to test the concept should be developed and prioritised, starting with a feasibility report in summer 2021, following in-depth scoping work:

- this should involve trustees and finance directors to test if they are prepared to run proof of concept trials and if it can provide sufficient learning for purposes of a real-world context and outcomes, with consideration of legal and other factors
- proof of concept trials offer opportunity for learning through testing administrative processes in the context of mass transfers and consolidation
- this includes, the prospect to investigate and test matching capability; use and development of data standards; the costs in the transfer process, in addition to end to end customer journey mapping and the appropriate safeguards necessary for members, with potential qualitative feedback gathered from those whose pots were consolidated
- in order to build beyond the proof of concept trials and ensure learnings are more broadly applicable, it requires the involvement of a wider group of stakeholders, including contract-based providers, consumer representatives and regulators
- consolidation system models can be prioritised, but final decisions should be informed and developed following the pensions industry's investigation and examination of administration processes and systems through an operational group. There are two automatic transfer and consolidation models that should be prioritised for low value small pots – the default small pot consolidation scheme ('default consolidator' including the various design choices) and the automatic pot follows member model.
- we recommend that the department, working with the pensions industry, should start to develop an initial costs/benefit analysis in the latter half of 2021 to help to further assess the models, including how these models complement pensions dashboards and reflect learning from the work on administrative processes to help better understand the VFM considerations, as far as evidence allows
- the pensions industry, working with the department, should develop customer journey mapping in relation to the models to understand the end to end process and to provide a deeper appreciation of the impacts, mindful of changes to the operating and delivery context

ROADMAP FROM THE SMALL POTS WORKING GROUP REPORT



ANNEX 2: MEMBERSHIP OF CO-ORDINATION GROUP AND WORKING GROUPS

CO-ORDINATION GROUP

NAME	ORGANISATION
Andy Cheseldine (Chair)	Capital Cranfield
Rob Yuille	ABI
Dale Critchley	Aviva
Gemma Mullis	Chartered Institute for Payroll and Pension Professional (CIPP)
Rob O'Carroll	DWP
Jasmine Smiley	Fidelity International
Tim Smith	Hebert Smith Freehills (HSF)
Zoe Alexander	NEST
Adrian Boulding	NOW: Pensions
Kim Gubler	PASA
Sarah Luheshi	Pensions Policy Institute (PPI)
Joe Dabrowski	PLSA
Ronnie Morgan	Royal London
Carol Knight	TISA
Philip Brown	The People's Pension (TPP)
Stephen McDonald	Which?
Observers	The Pensions Regulator (TPR) and Financial Conduct Authority (FCA)

DATA STANDARDS WORKING GROUP

NAME	ORGANISATION
Kim Gubler (Chair)	PASA
Evey Tang	ABI
Tom Davies / Mike Moore	DWP
Maurice Titley	ITM
Scott McLean	M&G
Ben Forsyth	NEST
Adrian Boulding	NOW: Pensions
Kate Boulden	PLSA
Ian MacIntyre	Royal London
Carol Knight	TISA
Karen MacKenzie	Which?
Richard Smith	Independent Consultant

TRANSFERS WORKING GROUP

NAME	ORGANISATION
Hetty Hughes (Chair)	ABI
Renny Biggins	TISA
Matt Burrell	Phoenix
Colin Clarke	L&G
Peter Cottingham	M&G
Dale Critchley	Aviva
Marc Davis	Hargreaves Lansdown
Nick Green	Criterion
Alyshia Harrington-Clark	PLSA
Ian MacIntyre	Royal London
David Moffatt	SS&C/DST
John O'Hara	Origo
Kevin Okell	Altus
David Pharo	PASA
Darren Philp	Smart Pension
Jacqui Reid	Sackers
Jasmine Smiley	Fidelity
Nathan Thompson	Aegon
Marie Walker	DWP
Matthew Zimmerman	Scottish Widows
Ben Forsyth	NEST

CONSUMER DETRIMENT WORKING GROUP

NAME	ORGANISATION
Stephen McDonald (Chair)	Which?
Hetty Hughes / Ben Infield	ABI
Rob O'Carroll / Tom Davies	DWP
Laurie Edmans	Financial Inclusion Commission
Francis McGee	Financial Services Consumer Panel
Tim Smith	HSF
Alyshia Harrington-Clark / Kate Boulden	PLSA
Sarah Luheshi	PPI
Darren Philip	Smart
Matt Burrell	Phoenix
Tim Gosling	The People's Pension
Lisa Leveridge	TPR

ANNEX 3: SMALL POTS CO-ORDINATION GROUP: TERMS OF REFERENCE 2021

CONTEXT / CHALLENGE

Automatic enrolment (AE) has successfully extended pension saving to millions of today's workers. Employers, pension scheme providers and private sector delivery partners throughout the supply chain have been central to its success.

Making workplace pension saving the norm, including for lower earners and people who move jobs frequently, and without active engagement being necessary, created a higher risk that an individual's pension savings would become fragmented in a number of small pension pots. The growth of deferred small pension pots presents significant challenges, in particular for savers and pension providers. Enabling consolidation could help to support greater personal ownership and empower people to understand and maximise their workplace pension savings.

Enabling widespread consolidation of multiple small pots will necessitate complementary solutions to the self-initiated transfers (which may increase given, for example, Pensions Dashboards).

In September the Department for Work and Pensions formed a cross-sector Working Group to examine the issue, prioritise options and provide an interim roadmap, with a package of actions and key considerations to tackle the growth of small pension pots. The final report was published in December 2020. Progress is now needed to implement the recommendations and take this work forward. This Co-ordination Group is constituted to take some of the next steps on recommendations forward.

ROLE AND PURPOSE OF THE CROSS-INDUSTRY SMALL POTS CO-ORDINATION GROUP

The purpose of the Co-ordination Group is to:

a) co-ordinate work to investigate and identify administrative challenges which will be necessary to underpin mass transfer and consolidation systems that can be delivered at scale within the AE market
b) co-ordinate the work of administrative working groups looking at different issues, e.g. matching, common data standards and low-cost bulk transfers, and set the objectives of those groups.
c) discuss the results of industry trials and feasibility study to align efforts on which concepts should be developed further and prioritised
d) produce a public summary of the above.

METHODOLOGY / GUIDING PRINCIPLES

To engage with interested parties and across sectors, with the aim of implementing the relevant recommendations as set out in the DWP Chaired Small Pots Working Group; and to identify any areas where additional government or legislative support/change may be needed to make progress.

To carry out further analysis of available and upcoming evidence, including consideration of behavioural insights and additional data.

When considering future work and progress, the group is mindful balancing costs and benefits for scheme members, pension providers and employers, and the trade-offs between the following guiding principles:

- Build on the success and behavioural insights of AE, and optimise retirement outcomes
- Promote value and transparency for savers
- Minimise administrative burdens for pension providers and employers (including SMEs)
- Support competition and a vibrant pensions market for members
- Fit with the direction of HMG's existing pension policies and reforms
- Maximise affordability and sustainability for members, employers, pension providers and tax-payers

OUTCOMES AND TIMING

The Group will prepare an update report in Summer 2021, which reflects the work of the group and progress made in implementing the recommendations in the Small Pots Working Group report.

RESOURCES

The PLSA will provide secretariat support for the group.

The Co-ordination group will meet at minimum once a quarter, with meetings planned in 2021 for March, May, June, September and November. Additional meetings will be determined by participants on an ongoing basis in line with need.

Relevant papers will be circulated at least seven days in advance of meetings and a note of key conclusions will be circulated within seven days following meetings. Formal paperwork will be kept to a minimum to reduce the burden of participation.

CONFIDENTIALITY

The principles under which information will be shared:

- Each member of the Group will treat any information shared within the group by other members which is not already available in the public domain as confidential and shall not disclose such information to any other person without obtaining the disclosing member's prior written consent, or use the information for any other purposes other than those set out in this agreement.
- The Group may share aggregate data; input/insights and findings from working groups with others in the co-ordination group, or government departments (including DWP and The Pensions Regulator) but where this data relates to provider data this will be combined into an anonymised picture so that no individual provider is identifiable.

COMPETITION LAW

All the work of the Co-ordination group will be undertaken in line with respective parties' competition policies.