Title: Impact Assessment on Occupational Pension Schemes (Charges and Governance) (Amendment) Regulations **IA No:** RPC-DWP-5108(1) **Lead department or agency:** Department for Work and Pensions	**Impact Assessment (IA)** **Date: 14/12/21** **Stage:** Final **Source of intervention:** Domestic **Type of measure:** Secondary legislation **Contact for enquiries:** Grace Cassidy (Analysis) Neil Walker (Policy)

Summary: Intervention and Options

Cost of Preferred (or more likely) Option (in 2020 prices)			
Total Net Present Social Value	**Business Net Present Value**	**Net cost to business per year**	**Business Impact Target Status**
-2.0	**-56.5**	**6.6**	Qualifying provision

What is the problem under consideration? Why is government action or intervention necessary?

The Government is committed to ensuring that individuals who are automatically enrolled into a pension scheme are protected from high and unfair charges and are saving into schemes that are well run. In 2015, a number of charge related measures were introduced to protect members. This included implementation of the charge cap of 0.75 per cent on administration charges in the default funds of Defined Contribution (DC) workplace pension schemes used for automatic enrolment. Under the charge cap there are three permitted charging structures:

a) a single percentage charge, capped at 0.75 per cent of funds under management annually;
b) a combination of a percentage charge on each contribution plus an annual percentage charge of funds under management;
c) a combination of an annual or monthly flat fee plus an annual percentage of funds under management charge.

Following the Work and Pensions Select Committee[1] meeting in 2019 on member borne charges in DC schemes, the Department for Work and Pensions (DWP) agreed to their recommendation to review the level and scope of the charge cap as well as the permitted structures. This included considering whether flat fees should be applied to deferred pension pots.

The combination charge, levying both a percentage charge and a flat fee, was of concern to the Committee, because flat fees can continue to be levied on a pot irrespective of whether a member is continuing to make contributions. This means that all deferred members, those not actively contributing to their pot, subject to flat fees could have their pots eroded over time. In the worst cases, where members have deferred, small pots, they may find their pot depleted to zero before they reach retirement.

As highlighted by the Small Pots Working Group report[2] making workplace pension saving the norm, especially for people who move jobs frequently, created an increased risk that an individual's pension savings could become fragmented into a number of deferred, small pension pots. Members with one or more deferred, small pension pots are at an increased risk of having their pot eroded by flat fee charges.

Building on this, there is an equity argument for intervening to protect those with pots at £100 or below. Those with multiple small, often deferred pots, are more likely to be those on low incomes and in more precarious forms of work. There is a body of evidence, such as that published by the Institute for Social and Economic Research and Joseph Roundtree Foundation[3], that explores the relationship between low pay and labour market churn, suggesting that those with higher numbers of small, deferred pension pots are more likely to be lower earners. Analysis from the Wealth and Assets survey supports this, suggesting that small, retained pots are found in highest numbers amongst females, those of lower earnings, and younger individuals (Table 7, 8 and 9). Flat fees placed on lower earners will be regressive and the introduction of a de minimis will therefore provide some protection against this.

What are the policy objectives of the action or intervention and the intended effects?

The policy objective is to limit the erosion of small pension pots by flat fee charges and prevent any members from being charged out entirely by flat fees, i.e. left with nothing in their pension pot.

The intended effect is to provide greater protection to the workplace pensions savings of members with smaller or deferred pots, where a flat fee may be charged. It should also ensure that those members' funds gain a degree of protection for when they reach retirement age. This policy is only applied to the savings of members who have not made an active choice on their fund and are therefore within the default arrangement.

[1] https://publications.parliament.uk/pa/cm201919/cmselect/cmworpen/292/29202.htm
[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945319/small-pots-working-group-report.pdf
[3] https://www.jrf.org.uk/sites/default/files/jrf/migrated/files/unemployment-pay-poverty-full.pdf
[4] https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Policy Option 0: Do nothing. This option would sustain and increase the issue of pot erosion as labour market churn continues to increase the volumes of deferred pots over time, which will be financially detrimental to pension scheme members and could cause reputational damage to the pensions industry. Without the de minimis the smallest pots will continue to be eroded by flat fees.

Policy Option 1: Introducing a £100 de minimis (preferred) on flat fees. Introducing secondary legislation to implement a de minimis pot size below which flat fees cannot be charged in default fund schemes. All other ongoing fees and charges continue to be applicable to these pots. We believe that a £100 de minimis strikes the right balance between tackling the issue of pot erosion for pension scheme members, whilst at the same time enabling the newer master trust pension schemes to maintain financial sustainability over the short term as their membership builds up and generates increasing revenue.

Policy Option 2: Introduce guidance around the erosion of smaller pots by flat fees. A non-mandatory policy option; issuing guidance to pension providers to encourage them to look at whether their members are at risk of pot erosion by flat fee charges. However, without regulation there is no obligation for providers who levy flat fees to follow this guidance so some members would still see their pots eroded to zero.

Our preferred option is Option 1 to ensure individual's pots are protected from erosion from charges. Options 0 and 2 would not ensure protection for members and would rely on action by the pension industry and only 2 providers have currently voluntarily adopted a de minimis on flat fees. Therefore, without intervention members pots would still be at risk of erosion which would negatively impact their future retirement accumulation and outcomes.

Will the policy be reviewed? It will not be reviewed. **If applicable, set review date:** Month/Year

Does implementation go beyond minimum EU requirements?		N/A			
Is this measure likely to impact on international trade and investment?		No			
Are any of these organisations in scope?	**Micro** Yes	**Small** Yes		**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)		**Traded:** N/A		**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: Guy Opperman Date: 24/11/2021

Summary: Analysis & Evidence — Policy Option 1

Description: Limiting the use of Flat Fees in Defined Contribution Pension Schemes – introducing a level or *a de minimis* where pension schemes cannot levy flat fees on members. This would apply to all members in qualifying workplace pension schemes in the default fund.

FULL ECONOMIC ASSESSMENT

Price Base Year 2019	**PV Base Year** 2020	**Time Period Years** 10 years	**Net Benefit (Present Value (PV)) (£m)**		
			Low: -51.1	**High:** 47.2	**Best Estimate:** -2.0

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	1.0		3.5	**31.4**
High	2.9		9.2	**81.5**
Best Estimate	2.0		6.3	**56.5**

Description and scale of key monetised costs by 'main affected groups'

Impact on business

As a result of the regulation, the relevant schemes in scope (Defined Contribution qualifying schemes used for automatic enrolment who levy flat fees on members in the default fund), henceforth "specified schemes" will be impacted in the following ways:

- One-off familiarisation cost to the "specified schemes" to read and understand the regulations
- One-off system changes and testing costs to enable "specified schemes" to update their systems to stop charging the affect pension pots
- One-off communication and marketing costs to notify employers and members of the changes to charges resulting from the implementation of the de minimis. There will also be a cost to update scheme documentation and literature, member communications and portals, and websites to reflect the changes to charges resulting from the implementation of the de minimis
- Ongoing loss of revenue by no longer charging flat fees to pots of £100 or less.

These costs will vary between different "specified schemes" depending on factors such as whether they are already operating a de minimis, the number of pots in scope, and the complexity of the systems that need updating.

Other key non-monetised costs by 'main affected groups'

Impact on regulators

We do not expect there to be any additional costs to the pension regulators or the Department. The cost of accommodating for the de minimis will be solely on providers and schemes. It is not our intention for the application of the de minimis to be part of any formal monitoring regime.

Impact on members

We cannot be certain how any additional costs for affected providers may be passed on to members. Providers may charge members with pots above £100 more, or alter their percentage charge applied to all members, to re-coup the loss in revenue.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	0		3.5	**30.4**
High	0		9.2	**78.6**
Best Estimate	0		6.3	**54.5**

Description and scale of key monetised benefits by 'main affected groups'

Impact on members

Members with pots of £100 or less and in schemes affected by the de minimis will save the flat fee amount each year until retirement. Members with multiple pots within the same provider will only benefit from the de minimis once.

No member should experience their pots eroded to zero after the introduction of the de minimis.

Small or deferred pot members

The introduction of a de minimis aims to protect the pension savings of members within schemes that levy a flat fee charging element. The Pension Charges Survey 2020[1] found the average flat fee ranged between £13 and £20 per annum and the highest flat fee levied was £36 per annum. This translated as an additional ongoing charge of between 0.14% and 0.22%. Members with pots in scope for the de minimis will save the flat fee amount each year until retirement.

Small pension pots, particularly deferred pots, can be eroded by charging structures quickly. Analysis from the Wealth and Assets Survey found 39% of the sample reported owning at least one pension pot(s) (Table 5). Moreover, 12% of the sample reported owning two or more pots and over 4% individuals reported having 3 or more pots (Table 5). Findings suggested small retained pots are found in highest numbers amongst females, those of lower earnings, and younger individuals (Table 7, 8 and 9).

The Pensions Policy Institute[2] estimates there are around 8 million deferred pension pots. This is expected to rise to as many as 27 million by 2035. The Pensions Policy Institute's[3] report into deferred pension pots noted a flat fee in combination with a percentage charge will leave a £100 deferred pot depleted within six years. This means that small deferred pots could, in a worst case scenario, have their pension pot entirely depleted by charges. The £100 de minimis is designed to limit pot erosion for these members and ensure that no member is left with a pot of zero.

Low earners

For members at the threshold for auto enrolment into a workplace pension schemes (£10,000 per annum), the average minimum monthly contribution (8%) would be around £25. The introduction of a £100 de minimis would fully protect around 4 to 5 months' worth of pension savings for the lower earners in auto enrolment; and provide partial protection beyond that in order to prevent their pots falling below £100.

Other key non-monetised benefits by 'main affected groups'

Reputation

Since the introduction of auto enrolment more people are saving into workplace pensions mainly in the DC Trust industry. It would negatively impact the reputation of the DC pension industry and workplace pensions if members' pots were entirely eroded by charges. However, the extent to which this is the case depends on whether people are fully aware of their pension pots.

Key assumptions/sensitivities/risks	**Discount rate (%)**	3.5%

[1] 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#contents

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

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

The majority of the data is from affected providers and is a point in time estimate of the number of pots under £100 (the stock of pots). This is a dynamic population, therefore, since the estimates were provided there may be more or fewer pots that are under £100, as existing members increase the value of their pots, and as new members join and begin contributing.

Providers will be affected in different ways depending on the proportion of pots they have under £100. Due to commercial sensitivity we can only provide aggregate figures of the impacts to business and we are reliant on our engagement with industry for the figures provided as the Department does not hold data on workplace pension pots by provider.

There may also be more providers in the market who levy flat fees on their members who we are not aware of.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £6.6m:						**Score for Business Impact Target (qualifying provisions only) £m:**
Costs:	**6.6m**	**Benefits: 0m**		**Net:**	**6.6m**	32.8

Evidence Base

The Policy Background

The Charge Cap

1. In 2015, the Government introduced the charge cap on all member-borne charges[4]. The charge cap applies solely to the default fund of defined contribution (DC) schemes used for automatic enrolment. It covers all member-borne administration charges associated with scheme and investment administration excluding transaction costs and a small number of other specific costs and charges. This was designed to protect members from unfair charges, deliver value for money and improve transparency of costs and charges.

2. The charge cap is set at 0.75% and there are three permitted charges structures:
   a) a single percentage charge, capped at 0.75 per cent of funds under management annually;
   b) a combination of a percentage charge for new funds when they are contributed to the pot plus an annual percentage charge for funds under management;
   c) a combination of an annual or monthly flat fee plus an annual percentage of funds under management charge.

3. The Pensions Regulator[5] estimate over 20 million members are in occupational DC schemes used for automatic enrolment and have therefore benefited from the introduction of the charge cap.

Flat Fee Charges

4. Different charging structures affect pension pots in different ways. There is evidence from the Pensions Policy Institute[6] that flat fees, whether alone or in combination with other ongoing charges, erode pots quicker than other charging structures (as seen in Table 1). This can have a significant impact on deferred pension pots in particular, which can be eroded to zero within a number of years. Small active pension pots can also be impacted by flat fees. Unlike deferred pension pots where there are no on-going contributions, an active pension pot may still grow due

---

[4] http://www.legislation.gov.uk/uksi/2015/879/contents

[5] https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2019-2020

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

to member and employer contributions, but a flat fee may take away a large proportion of any growth for small pension pots.

Table 1: The Pensions Policy Institute modelling of different charging structures on deferred pot sizes

Charging structure	Pot size at age 68					
	Deferred at age 22			Deferred at age 40		
	£100	£500	£1,000	£100	£500	£1,000
Baseline – no charge	£300	£1,500	£3,000	£200	£1,000	£1,900
0.5% AMC only	£200	£1,200	£2,400	£200	£800	£1,700
£20 annual flat fee and 0.25% AMC	£0	£100	£1,400	£0	£200	£1,100
£24 annual flat fee only	£0	£0	£1,400	£0	£100	£1,100

Source: The Pensions Policy Institute[7]

5. The impacts of flat fees on pension pots will vary depending on the size of the flat fee, the rate of investment growth, the level of member and employer contributions, and the size of the pension pot.

6. Within the DC pension industry, small pension pots affect both pension providers and members. For providers, the cost of servicing small pots can be in excess of the pot-level revenue generated by just a percentage charge. For members there is a risk their small pot can be eroded by charges, especially if the member is no longer paying into the pot. For members with more than one small pension pot, it could be possible that they could be subject to multiple pot erosion across different providers. This is a risk for the reputation of the pension industry and workplace pension saving if members see their pots depleted entirely and lose confidence in pension saving.

7. The DC pensions market is still relatively immature and some providers are still in the process of repaying start up loans. The Pensions Policy Institute's[8] report on Master Trust sustainability found the greatest challenge to the financial sustainability of master trusts is the need to cover initial start-up and running costs until levels of membership and assets have grown sufficiently. Therefore these providers must balance delivering value for money for their members and their financial sustainability going forward.

8. Evidence from the DWP Charges Survey 2020[9] indicates that on average, the fees charged to members are low and that this is due to competition in the market. Setting the de minimis too high could reduce competition in the future, worsening outcomes for members on average.

Rationale for Intervention

9. The Government is committed to ensuring that individuals who are automatically enrolled into a workplace pension scheme are protected from high and unfair charges and are saving into schemes that are well governed. This includes ensuring pension scheme members get value for money from their workplace pensions.

10. In 2019, the Work and Pensions Select Committee[10] heard evidence on charges in DC schemes and recommended the DWP review the level and scope of the cap as well as the permitted structures. This included considering whether flat fees should be applied to deferred pension pots.

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

[8] https://www.pensionspolicyinstitute.org.uk/media/3590/20200827-ppi-financial-sustainability-of-master-trust-schemes-final.pdf

[9] 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

[10] https://publications.parliament.uk/pa/cm201919/cmselect/cmworpen/292/29202.htm

11. The combination charge, levying both a percentage charge and a flat rate fee, is of concern because flat fees can continue to be levied on a pot irrespective of whether a member is continuing to make contributions. This of particular concern for individuals who have one or more small pension pot.

12. As noted in the Small Pots Working Group report[11], making workplace pension saving the norm, especially for people who move jobs frequently, created an increased risk that an individual's pension savings could become fragmented into a number of deferred, small pension pots. In 2012, the Department[12] estimated that employees work for 11 employers on average during their working life (with a quarter working for more than 14 employers). More recent estimates from external research studies[13] suggest that people aged 18 - 34 may expect to have an average of over 12 jobs in their lifetimes. The ONS[14] estimate that around nine per cent of people changed jobs each year between 2000 and 2018 on average, reaching a high of 10.9 per cent in 2018 further demonstrating the extent of churn in the labour market. Whilst in some cases new employees may be automatically enrolled into schemes where they already have an existing pot, the estimated frequency of job moves combined with the large number of providers in the DC market (from which employers are free to choose) makes the accrual of several small pots through changing jobs a likely reality for many savers.

13. Without further intervention, flat fees would continue to be charged on smaller pension pots and risk these being eroded further. In the worst cases, this may lead to some pots being eroded to zero and without intervention, these people with small pension pots would continue to see their pots eroded which negatively impacts their future income as a pensioner.

14. Building on this, there is an equity argument for intervening to protect those with pots £100 or below. Those with multiple small, often deferred pots, are more likely to be those on low incomes and in more precarious forms of work. There is a body of evidence, such as that published by the Institute for Social and Economic Research[15] (ISER) and Joseph Roundtree Foundation (JPF), that explores the relationship between low pay and labour market churn, suggesting that those with higher numbers of small, deferred pension pots are more likely to be lower earners. For example, the JFR report on low pay found One aspect of low-paid work that is particularly concerning is its link to employment insecurity. Those working for low wages tend to also be working in jobs characterised by temporary contracts and low hours.

15. Moreover, analysis of the Wealth and Assets Survey (WAS) supports this, suggesting that small, retained pots are found in highest numbers amongst females, those of lower earnings, and younger individuals (Table 7, 8 and 9). Flat fees placed on lower earners will be regressive and the introduction of a de minimis will therefore provide some protection against this.

16. As well as deferred pension pots, small active pension pots may see some or all of their growth eroded by flat fees.

17. The consultations on the Review of the Default Fund Charge Cap and Standardised Cost Disclosure[16] and Permitted charges within Defined Contribution pension schemes[17] outlined the intention to limit the risk of erosion to their pension savings from flat fees. As a result, it was announced that a minimum level (or *de minimis*) would be introduced before a flat fee element of

---

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

[12] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/184965/small-pots-automatic-transfers-impact-assessment.pdf

[13] https://www.recruitment-international.co.uk/blog/2017/11/millennials-likely-to-have-12-jobs-in-their-working-lives-research-finds

[14] https://www.ons.gov.uk/economy/nationalaccounts/uksectoraccounts/compendium/economicreview/april2019/analysisofjobchangersandstayers

[15] https://www.iser.essex.ac.uk/research/publications/523273

[16] https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure#standardised-cost-disclosure-templates

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

a charging structure could be applied to a member's rights (that's is the total value of their savings pot or pots).

18. To assess the impact of the de minimis we have used evidence from:
    - The Pension Charges Survey 2020
    - Wealth and Assets Survey
    - Data from the Small Pots Working Group
    - Analysis from the Pensions Policy Institute
    - Conversations with the industry
    - And responses to the Permitted charged within Defined Contribution pension schemes[18] consultation

Description of options considered

Policy Option 0: Do nothing

19. The Government has considered the option of not introducing regulation to limit the application of flat fees on pots of £100 or less. However, there are several reasons why the 'Do Nothing' option is not preferred.

20. If no de minimis is introduced some pension pots subject to flat fees will continue to be eroded. Whilst this would require no new regulation and pension schemes would not have to make any changes to their charging structures or governance, it does not prevent pots from being gradually eroded or fully charged out.

21. The charge cap introduced through the Occupation Pension Schemes (Charges and Governance) Regulation 2015[19] provides a level of protection to members and prevents a range of unfair charging structures. However, there is evidence of member's pots being eroded despite the charge cap. For example many responses to the Review of the Default Fund Charge Cap and Standardised Cost Disclosure[20] and Permitted charges within Defined Contribution pension schemes[21] suggested that flat fee charges could lead to pension scheme members being in a position where they can lose all of their pension savings.

22. There would be no cost to business through this option although there would also be no benefit for members.

Policy Option 2: Introduce guidance around the erosion of smaller pots by flat fees.

23. The Government has also considered a less comprehensive non-mandatory policy option; issuing further guidance to schemes on how to take into account whether their members are at risk of pot erosion by flat fee charges.

24. This option would not confer any new responsibilities or duties on occupational pension schemes. Instead the guidance would be published by the Department with the objective of encouraging schemes to consider the impact of flat fees on small pension pots.

25. However, the lack of statutory weight behind the guidance would be unlikely to result in the level of compliance and implementation that the policy objective requires. There would be no obligation for

---

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

19 http://www.legislation.gov.uk/uksi/2015/879/contents

20 https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure#standardised-cost-disclosure-templates

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

providers who levy flat fees to follow this guidance so some members would still see their pots eroded to zero. An example of this, as referenced in a previous Impact Assessment[22], is non-statutory guidance from The Pensions Regulator (TPR) in the Defined Benefit Funding Code of Practice. TPR research found that 92% of trustees interviewed stated they had read the DB code of practice or a summary of it provided by the adviser. However, only 64% of trustees stated they had carried out all five of the activities.

26. We estimate the only cost to business for Option 2 to be one-off familiarisation with the new guidance.

Familiarisation for Option 2

27. Only those "specified schemes" who levy flat fees would be expected to familiarise themselves with the regulations.

28. There would be one-off costs to all the 'specified scheme' trustees to familiarise themselves with the new guidance.

29. We assume that it would take all trustees of in-scope schemes approximately 3.5 hours to read and understand a 35-page guidance document. We have assumed it would take around 6 minutes to read each page, based on previous impact assessments[23].

30. We have estimated that schemes in scope of the proposed requirements will have approximately 6 trustees per scheme, based on our engagement with industry, with an estimated average hourly cost (including overheads) of £100 per hour.

31. These total one-off costs to all schemes in scope are estimated to be £12,600.

Familiarisation with exact requirements

6 providers in scope x 3.5 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £12,600

32. If "specified schemes" then decided based on the guidance to implement a policy to deal with the erosion of small pots by flat fees this would be an optional cost and is therefore not included here.

Policy objective

33. The policy objective is to limit the erosion of small pension pots by flat fee charges and prevent any members from being charged out entirely by flat fees. Although there needs to be a balance between protecting members, especially those with small pots, and maintaining the financial sustainability of schemes, it is important to maintain public confidence in automatic enrolment and workplace pension saving.

34. As evidenced by the PPI report into financial sustainability, the DC pensions market is still relatively immature and some providers are still in the process of repaying start up loans. These providers must balance delivering value for money for their members and their financial sustainability going forward.

Preferred Option (Option 1) – De minimis on flat fees

35. Our preferred option is the introduction of a level or de minimis where providers can no longer charge flat fees on the smallest pots. This will apply to all members in the default fund of qualifying schemes used for workplace pensions and will be set at £100. Where a member's

[22] https://publications.parliament.uk/pa/bills/lbill/58-01/004/5801004-IA-Annex-E.pdf

[23] https://www.gov.uk/government/consultations/improving-outcomes-for-members-of-defined-contribution-pension-schemes/impact-assessment-default-sip-for-schemes-with-a-default-fund-that-is-with-profits

rights (i.e. the sum total of their pension pot or pots with a provider) is at £100 or below, then no flat fee could be charged to that member.

36. We intend to introduce secondary legislation to amend the Occupation Pension Schemes (Charges and Governance) Regulation 2015[24]. The Government intends to implement this change from April 2022.

Monetised and non-monetised costs and benefits of each option

	Option 0: Do nothing	Option 1: £100 de minimis	Option 2: Guidance only
Familiarisation	Not applicable	£13,300	£12,600
System Updates	Not applicable	£1,650,000	Optional
Communications	Not applicable	£290,000	Optional
Foregone revenue (per year)	Not applicable	£6,330,000	Optional

Direct costs and benefits to business calculations

Costs to Pension Schemes in Scope

37. During the process of estimating the potential costs to pension schemes, the Department has engaged with the UK pensions industry via the Permitted charges within Defined Contribution pension schemes[25] consultation and directly with known affected providers.

38. The proposed elements of costs are divided into:
    - One-off familiarisation cost to the "specified schemes" to read and understand the regulations
    - One-off system changes and testing costs to enable "specified schemes" to update their systems to stop charges being applied to the affect pension pots
    - One-off communication and marketing costs to notify employers and members of the changes to charges resulting from the implementation of the de minimis. Additional costs to update scheme documentation and literature, member communications and portals, and websites to reflect the changes to charges resulting from the implementation of the de minimis
    - Ongoing loss of revenue by no longer charging flat fees to pots of £100 or less.

Year	2021/2022	2022/2023 – 2030/2031
Appraisal period year	1	2-10
Event	Regulations laid (December 2021) De minimis comes into force	De minimis in place
Cost	Familiarisation with secondary legislation and guidance System updates Implementation Communication and marketing costs	Ongoing loss of revenue on any future pots of £100 or less

[24] http://www.legislation.gov.uk/uksi/2015/879/contents

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

	Initial loss of revenue	
Benefit	Members with pots of £100 or less do not incur flat fees	Members with pots of £100 or less do not incur flat fees

39. The analysis in this section is based on engagement with industry, with cost information shared with us from all the “specified schemes”. This is commercially sensitive information which is not suitable for publication.

Familiarisation

40. Only those “specified schemes” directly affected by the de minimis will be expected to familiarise themselves with the regulations.

41. There would be one-off costs to all the ‘specified scheme’ trustees to familiarise themselves with the new regulations. A pension scheme in scope will experience this one-off cost in the first year only.

42. We estimate that it would take all trustees of in-scope schemes approximately 3.7 hours to read and understand the regulations and guidance. We have assumed the regulations are 2 pages and the guidance is 35 pages. We have assumed it would take around 6 minutes to read each page, based on evidence used within previous impact assessments[26].

43. We have estimated that schemes in scope of the proposed requirements will have approximately 6 trustees per scheme, based on our engagement with industry, with an estimated average hourly cost (including overheads) of £100 per hour.

44. These total one-off costs to all schemes in scope are estimated to be £13,300.

Familiarisation with exact requirements

6 providers in scope x 3.7 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £13,300

System updates

45. Based on discussions with “specified schemes” we expect there will be a one-off administrative cost to “specified schemes” of stopping pots of £100 or less being charged flat fees. This one off administrative cost will entail:
    - Planning and development of system changes required to adhere to the de minimis;
    - Testing any changes made to the system.

46. This cost will vary between different “specified schemes” depending on factors such as whether they already operate a de minimis or the complexity of the systems that need updating. From industry engagement, we know that two affected schemes operate a de minimis and we expect their system updating costs to be minimal.

47. This cost will involve trustees, senior managers, IT and software resource. Systems will need to be updated to prevent pots £100 or less being charged the flat fee. Any changes to these systems will require testing.

[26] https://www.gov.uk/government/consultations/improving-outcomes-for-members-of-defined-contribution-pension-schemes/impact-assessment-default-sip-for-schemes-with-a-default-fund-that-is-with-profits

48. Providers can manage their schemes internally or via a third party. For a scheme with good data management and platforms, they may be able to identify these pots quickly and make the necessary changes without incurring excessive additional costs. However, schemes who use third-party platforms may have to pay to amend their contract or ask their contractor to take on additional work.

49. Based on engagement with industry and consultation responses, our estimate of the aggregate costs to “specified schemes” is £1.65 million. Due to commercial confidentiality and the agreements with which these costs were shared with us by the “specified schemes”, we are unable to publish any additional details on these costs.

System updating costs
Best estimate = £1,650,000

50. Some “specified schemes” also outlined there may be additional ongoing testing of the system in the future. However, this is optional and part of the running costs of pension administration regardless of the implementation of the de minimis. Therefore, we have not included this within our costs to business.

Communication and Marketing costs

51. We estimate there will be a one-off communication cost to “specified schemes” to notify employers and/or members about the changes to charges resulting from the implementation of the de minimis. This cost will vary between different “specified schemes” depending on factors such as whether they already operate a de minimis or how they choose to notify members. For example, sending a letter to all members is likely to be more expensive than emailing. Some “specified schemes” outlined they may not be able to contact deferred members.

52. One ‘specified scheme’ outlined that they expect some increased member queries and engagement following the implementation of the de minimis although they are not able to quantify what these cost may be.

53. Some “specified schemes” outlined that notifying members of the de minimis coincided with other regular member communications and therefore the additional cost was negligible.

54. As well as communicating directly with employers and/or members, “specified schemes” will be required to update supporting materials. This may include, but is not limited to:
    - Updating charges information on websites
    - Updating member portals
    - Updating scheme documentation and literature
    - Updating benefit annexes and employer information.

55. This change may involve communication or marketing colleagues’ time to work out where changes are needed. Then new content must be created which will then be signed off by trustees. There is also additional time to update the communications once signed off. Engagement with industry said it was often hard to distinguish the communication and marketing costs.

56. Based on engagement with industry and consultation responses, our estimate of the aggregate costs to “specified schemes” is £290,000. Again, due to commercial confidentiality and the agreements with which these costs were shared with us by the “specified schemes”, we are unable to publish any additional details on these costs.

Communication costs
Best estimate = £290,000

Foregone revenue in year 1

57. We estimate there will be ongoing loss of revenue to "specified schemes" going forward as they will no longer be able to levy flat fees on pots worth £100 or less.

58. To calculate loss of revenue we need to know the number of pots worth £100 or less that are subject to flat fees and the flat fee that is levied. This is commercially sensitive information which is not suitable for publication. Where appropriate we have used aggregate figures to outline the number of pots affected the loss of revenue.

59. Once the regulations come into force, for providers charging a flat fee it may only be levied to the extent that it would not reduce the value of the member's rights to below £100. Therefore, providers will also lose revenue on some pots worth over £100 due to only being able to charge a partial flat fee to bring the pot size down to, but not below, the level of the de minimis. We are unable to estimate the number of pots that this applies to nor the lost revenue from this due to lack of sufficiently granular data. The data we have been able to gather from providers is based on aggregate figures of members for specific pot value bands.

60. However, not all of the pots worth £100 or less that were provided to us by the "specified schemes" will currently be subject to the flat fee. According to existing legislation, providers are only permitted to levy a flat fee on an individual once regardless of the number of pots they may hold with that provider. As there are a small number of large master trusts and they tend to have strong links with particular sections of the labour market it is likely that as individuals move jobs they will repeatedly be enrolled into pensions with the same providers. Research by the Pension Policy Institute[27] found that this could be in the region of 20% to 50% of deferred pots. This would therefore reduce the estimate of total forgone revenue by between 20 and 50%. From engagement with industry there may be operational reasons as to why members' pots cannot be matched and therefore some members may be charged flat fees on more than one pot under current legislation. However, we do not have any evidence as to the extent of this. This would be expected to lower the 20-50% estimate.

61. Finally, any revenue loss could be partially or fully off-set by providers increasing flat fees for those above the de minimis or by increasing percentage charges applied to all members. Evidence from the DWP Charges Survey 2020 suggests that on average, charges are low across the DC market, and that competition between providers is a significant factor in driving down average charges.

.

62. Based on the information provided to us by the six "specified schemes" our best estimate of the number of pots worth £100 or below that are subject to flat fees is 1.5 million. This was a point in time estimate of a dynamic population, therefore we would expect this estimate to have changed since our data request. We are unable to quantify this uncertainty, but it is explored further in the next section as it becomes more meaningful over time.

63. From the information provided throughout this section, our best estimate of the loss of revenue on these pots is therefore £6.33 million.

Foregone revenue
Best estimate = £6,330,000

Loss of revenue (going forward)

64. As one respondent noted in their consultation response:
"In the short term, the de minimis may help with the stock of small pots from being eroded to zero, however, it will not do anything to prevent the flow or creation of small pots".

65. As noted above, this is a dynamic population, so we would not expect the estimate of the number of pots impacted by the policy change to remain at 1.5m over time.

66. There are two main ways in which this number of pots could increase:

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

a) from new pots of £100 or less being created by new members of pension schemes who charge flat fees;
b) from pots of over £100 with providers who charge flat fees falling to £100 or less and becoming subject to the de minimis.

67. Similarly, there are three main ways in which the number of pots subject to the de minimis could fall over time:
    c) from pots growing to above £100 through contributions from the employee and employer, and/or investment growth;
    d) from pots being moved to a provider who does not charge a flat fee;
    e) from deferred pots of £100 or less being charged out to zero and no longer attracting a flat fee.

68. Further data and evidence on each of these is laid out below to inform whether we think the overall stock of pots of £100 or less would be expected to increase or decrease over time.

69. Firstly, internal DWP analysis of HMRC RTI data shows that the average monthly number of eligible employees starting to save into a workplace pension each month was around 375,000 in 2021. As shown in Table 2 this was a slight increase from the average in 2020, but a slight decrease from 2018 and 2019. Due to the staged approach in which Automatic Enrolment was introduced some (mainly micro) employers reached their staging date in 2018, meaning we would expect slightly higher numbers that year. Due to the impacts on the labour market of the SARS-CoV-2 pandemic we would expect the number of employees starting new jobs and saving into a pension each month to be lower on average in 2020 and 2021.

Table 2: Average number of eligible employees starting saving into a workplace pension each month

	2018	**2019**	**2020**	**2021**
Average monthly inflow	415,000	410,000	340,000	375,000

Source: DWP estimate derived from HMRC Real Time Information (RTI) data

70. Data from the Pensions Regulator[28] shows that in 2020/21 memberships of non-hybrid DC master trusts was 18.6 million, up from 16.3 million in 2019/20, an increase of about 2.3 million memberships[29]. Not all new memberships will be in the Master Trusts who charge flat fees, and this data does not provide information on the size of pension pots for these new memberships.

71. In order to estimate how many new pots created each month would be of £100 or less we conducted analysis of ASHE data on the amount of employer and employee contributions to DC pensions. We were unable to do this for just new DC pension pots and so the numbers include contributions to existing pots as well. This analysis showed that of all people saving into a DC pension pot in 2020 91% had monthly employer and employee contributions of over £100, meaning the pot would not have been subject to the de minimis at all. Of the remaining 9% of people, around 5% would have contributions that reached above £100 in two months, 2% would have reached over £100 in three months and the remaining 3% would have reached it in four or more months. Assuming this level of contributions is reflected in those starting saving into a workplace pension this would suggest that only a minority of new pots would be subject to the de minimis each month.

72. Secondly, pots that are worth over £100 are at risk of erosion over the appraisal period and may become subject to the de minimis, especially if investment performance was particularly poor. However, the likelihood of negative returns is relatively low. The Barclays Equity Gilt Study 2020[30] looked at the distributions of investment returns over the last 120 years and the largest single year fall in that period was 50%. Therefore, in the worst case scenario, pots between £100 and £200 could be at risk. This risk is likely to be higher on deferred pots who are solely reliant on investment

[28] https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2020-2021#56a3fa2c08c44eaab6b7367f5f49b39e
[29] The number of memberships does not equate to the number of individuals, as one individual can have multiple memberships.
[30] https://home.barclays/news/2021/05/The-economics-of-the-new-normal/

performance for growth. However, the same study showed that over the sample period, the worst average annualised 10-year return for equities was around -5%, while the best was over +15%.

73. Moreover, Pensions Policy Institute[31] modelling has assumed investment returns are around 5.3%, in line with the Office for Budget Responsibility's (OBR) forecast of asset yields from the Economic and Fiscal Outlook (EFO). Similarly, Corporate Advisor[32] analysis shows that for Master Trusts there was an average annualised 5-year return of over 6% in the most recent data.

74. In terms of how many pots of £100 or less and subject to the de minimis are likely to grow to over £100 and move beyond the scope of the de minimis, the above analysis has shown that for the vast majority of active pots this is likely to happen within a couple of months. For deferred pots due to the lack of contributions any growth will only be due to investment performance, which wouldn't be expected to be above the flat fee charge.

75. We do not have a good estimate of the number of pots that are subject to the de minimis that might be moved to a provider who does not charge a flat fee. The Small pots working group report[33] looked at member-led solutions to the issue of small pension pots and concluded that due to low member engagement with their pensions they unlikely to engage in the consolidation process and move their pension pot to another provider.

76. Finally, in terms of how many deferred pots might be eroded to zero and therefore stop being chargeable, again, we do not have granular enough data to estimate this. On average, we would expect flat fees net investment growth to be around £10-£15 per annum for pots between £0-£100. If pots below £100 were evenly distributed, we might therefore expect up to 15% of deferred pots to be charged out to zero per annum.

77. Due to the lack of evidence on the overall balance of these dynamics to inform how many pots are expected to be subject to the de minimis in future years, our best assumption is that the current figure of 1.5 million pots stays roughly stable over the ten-year appraisal period. Therefore, the loss of revenue from no longer being able to charge a flat fee on these pots will also be the same for each year.

Sensitivity Analysis

78. For familiarisation, assuming a 50% decrease or increase in the hours a trustee takes to familiarise themselves with the regulation and guidance our estimates are:

Familiarisation with exact requirements (Best estimate)
6 providers in scope x 3.7 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £13,300

Familiarisation with exact requirements (Low estimate)
6 providers in scope x 1.58 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £6,700

Familiarisation with exact requirements (High estimate)
6 providers in scope x 7.5 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £20,000

31 https://www.pensionspolicyinstitute.org.uk/media/3828/20210609-ppi-adequate-retirement-income-report.pdf?utm_medium=email&utm_campaign=PUBLISHED%20TODAY%20What%20is%20an%20adequate%20retirement%20income&utm_content=PUBLISHED%20TODAY%20What%20is%20an%20adequate%20retirement%20income+CID_ec2261e8506649931e3d48aa1d57cfbd&utm_source=Email%20marketing%20software&utm_term=To%20download%20the%20report%20plese%20click%20here

32 https://corporate-adviser.com/master-trust-gpp-report-46pc-difference-in-5-year-returns-schemes-defy-pandemic/

33 https://www.gov.uk/government/publications/small-pension-pots-working-group/small-pots-working-group-report#chapter-3--member-led-solutions--analysis-and-recommendations

79. We could also assume, for our high estimate, that all pension schemes regardless of whether they levy flat fees may need to familiarisation themselves with the regulations. We don't think this is meaningful as we expect that Trustees will know what a flat fee is and judge quickly whether they are impacted or not. Flat fees are already a part of the permitted charging structures that Trustees have to operate within. However, for illustrative purposes, using TPR's[34] data of the number of DC schemes, our best estimate for this scenario is:

Familiarisation with exact requirements (High estimate – all schemes)
28,360 schemes x 3.7 hours spent familiarising x 6 trustees at provider x £100 trustee wage = £62,960,000

80. For systems changes and testing costs, assuming a 50% decrease or increase in the cost of updating any systems our estimates are:

System updating costs
Best estimate = £1,650,000
Low estimate = £825,000
High estimate = £2,475,000

81. Moreover, the estimates of system changes and testing costs ranged significantly between providers with some require more or less extensive work to be undertaken than others. Some providers suggested these costs were within their existing their existing contracts so did not incur a significant additional cost. It was also raised that because the de minimis is a statutory change they did not see this an additional cost but as a necessity to running the pension scheme legally. We have also included estimates accounting for potential optimism bias using the standard Green Book optimism bias[35] recommended adjustment ranges for equipment or development projects. However, given that providers thought the majority of costs were mainly covered by existing contracts and work plans it's likely the risk of optimism bias is low.

System updating costs (optimism bias)
Upper estimate = £1,650,000 + (200% x £1,650,000) = £4,950,000
Lower estimate = £1,650,000 + (10% x £1,650,000) = £1,815,000

82. For communication and marketing costs, assuming a 50% decrease or increase in the cost of updating any systems our estimates are:

Communication costs
Best estimate = £290,000
Low estimate = £145,000
High estimate = £435,000

83. Similarly to the system updating costs, providers estimated a range of costs. Some providers suggested the costs of updating marketing and communication were difficult to estimate as they were part of the day-to-day running costs and therefore didn't incur large additional costs. However, most were able to provide us with an aggregate figure of cost. We have also included estimates accounting for potential optimism bias using the standard Green Book optimism bias[36] recommended adjustment ranges for equipment or development projects. Given most providers felt these costs fell within the day-to-day running of the scheme, the risk of optimism bias is low.

Communication costs (optimism bias)
Upper estimate = £290,000 + (200% x £290,000) = £870,000
Lower estimate = £290,000 + (10% x £290,000) = £319,000

---

[34] https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2020-2021
[35] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/191507/Optimism_bias.pdf
[36] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/191507/Optimism_bias.pdf

84. For future forgone revenue costs, assuming a 50% decrease or increase in the future foregone revenue:

Future foregone revenue costs
Best estimate = £6,330,000
Low estimate = £3,170,000
High estimate = £14,610,000

Non-monetised costs

Cross-subsidy

85. The Pensions Policy Institute[37] defines cross-subsidies as a member paying more in charges than the costs incurred on their behalf, while at the same time a different member pays less in charges than the costs they incur.

86. Cross-subsidies exist within all charging structures but are more common in single percentage charging structures. Using a flat fee can help reduce some of the cross-subsidy between larger and smaller pots.

87. The Pensions Policy Institute[38] found in a Master Trust that uses a proportion of fund charge, smaller pots are subsidised by larger pots. Inactive pots tend to be smaller than active pots. The increase in the ratio of inactive pots to active pots increases the extent to which active pots may need to support the inactive pots. This type of cross-subsidy could increase if schemes can no longer charge flat fees on pots of £100 or less. This could be viewed as unfair to members who are continually saving into their pension pots having their contributions used to preserve the pots of others.

88. A number of consultation responses highlighted that charges on small pots are predominantly to cover the cost of administering them; and that with the introduction of the de minimis this cost will need to be absorbed or redistributed across other pots if the provider does not or cannot absorb the revenue loss. This could be through increasing the flat charge above the level of the de minimis resulting in other members cross-subsidising smaller pot members.

89. We cannot be sure how the added costs or loss in revenue to some providers may be passed onto members. Given that all members of qualifying schemes are below the cap and the average charge is fairly low, it could result in charges for members with pots larger than £100 increasing to subsidise the de minimis or the percentage charge rising for all members. Trustees have a fiduciary duty to act in the best interests of all their members and such changes would be made in the light of that overall duty. Without any concrete evidence we have been unable to calculate this potential impact.

90. According to a Pensions Policy Institute[39] report on Master Trust financial sustainability their annual expenditure has been growing year on year, with cumulative expenditure around £1 billion by 2019 and costs expected to continue to grow. The report also found the Master Trust industry is unlikely to achieve breakeven on costs until around 2025 and the potential loss in revenue may push this back further for the affected Master Trusts unless they increase their charges. Financial sustainability is a challenge for automatic enrolment providers and delaying paying back their loans may affect Master Trust ability to scale their assets, pursue innovation and prepare for future challenges and regulation.

91. In their consultation response, one respondent noted:

---

[37] https://www.pensionspolicyinstitute.org.uk/media/3263/20190911-pension-charging-structures-and-beyond.pdf

[38] https://www.pensionspolicyinstitute.org.uk/media/3263/20190911-pension-charging-structures-and-beyond.pdf

[39] https://www.pensionspolicyinstitute.org.uk/media/3590/20200827-ppi-financial-sustainability-of-master-trust-schemes-final.pdf

"For a minority it will also have an implication for their investments, and on their charging model. For example, the whole charging structure of the provider may need to be evaluated to ensure financial sustainability and this could result in higher charges for other members."

92. However, as noted in the report Master Trusts are growing and the industry is nearing the point of breakeven. The majority of Master Trusts do not charge flat fees and so will not be impacted by this measure. The Pension Charges Survey 2020[40] also found that pension providers felt under pressure to maintain low charges due to competitive pressure. This suggests that pension schemes may not necessarily raise charges on other members in order to pass on the costs of no longer being able to charge flat fees for pension pots of £100 or less.

Consolidation

93. Responses to the Review of the Default Fund Charge Cap and Standardised Cost Disclosure[41] and Permitted charges within Defined Contribution pension schemes[42] consultations suggested the introduction of a de minimis may disincentive members from consolidating their smaller pots as they are at less of a risk of pot erosion.

94. For example, one respondent suggested:
"Removal of the flat fee may be a disincentive for members to engage with their small pension pot and consolidate into a more modern pension pot offering better value for money".

95. A greater number of small pots due to reduced consolidation could mean more cross-subsidisation of pots and more less revenue for providers.

Opportunity Cost

96. In our engagement with industry, it was highlighted that in order to implement the de minimis other work may have to be put on hold or postponed. Implementation requires the time of trustees, marketing and IT support at a minimum. Therefore, there may be other projects or innovation which are not pursued in order to meet the regulatory requirements of the de minimis. Some of these may have been beneficial to both the provider and members.

Benefits to Pension Schemes

Reputation

97. It is damaging to the success and reputation of auto enrolment and the workplace pension industry if members have their pots eroded significantly by charges. By ensuring members' pensions are protected from excessive charges it should help limit pot erosion and maintain the reputation of the DC pension industry.

98. Whilst we cannot quantify this benefit, it is generally accepted that saving into a workplace pension is a beneficial choice for the majority of the working-age population. If the reputation of automatic enrolment was damaged by charging out it would undermine the key purpose of workplace pensions: to get people saving for retirement.

Benefits to Members

Savings to affected members

---

[40] 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#contents

[41] https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure#standardised-cost-disclosure-templates

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

99. We estimate there will be ongoing benefit to members with pots £100 or less who will no longer be charged flat fees. Our best estimate of the number of pots £100 or less that are subject to flat fees is 1.5 million. We refer to pots rather than number of people because it is possible for someone to own more than one pot and therefore benefit from the saving more than once.

100. Our best estimate of the savings to members is £6.33 million each year.

Risks and assumptions

Assumptions for flat fees

101. The Pension Charges Survey 2020[43] found four out of the 20 providers interviewed levied a flat fee, of which three were trust-based schemes so within the scope of these regulations. However, some providers have adopted a flat fee since the survey was conducted.

102. Therefore, we have assumed based on Pension Charges Survey 2020[44] and response to our consultations that there are at least six providers who may be impacted, although some of these providers do not levy flat fees on all members.

103. We assume the introduction of a de minimis would have a limited impact on the biggest providers, as the flat fee charging structures is still in the minority across DC large providers. However, it is worth highlighting some of the "specified schemes" are newer Master Trust associated with the "heavy-lifting" of automatic enrolment (meaning those Master Trusts who have taken on administering pension schemes for a higher proportion of lower earners automatically enrolled into pension saving for the first time). These schemes are newer and paying back set up loans whilst building their assets. These schemes are more likely to have taken on smaller pots and service a large proportion of the automatic enrolment market.

104. The Pension Charges Survey 2020[45] found the average flat fee ranged from £13 to £20, with the highest fee found at £36. Flat fees charged by affected providers range from between £2.50 per annum to £24 per annum.

105. Responses to our consultation and engagement with industry highlighted costs are likely to vary between providers. For example, two providers already have adopted a de minimis and therefore costs for these providers are likely to be lower.

Assumptions for familiarisation

106. We have assumed only "specified schemes" within the scope of the regulations will need to familiarise themselves regardless of whether the de minimis will directly affect their charging structure. We estimate there is 6 providers who will be affected.

107. We have assumed an average cost of an hour of time for a Trustee is £100 per hour, this is based on engagement with the industry and previous pensions impact assessments[46].

108. We also assumed approximately 6 trustees per scheme, based on engagement with the industry.

109. For familiarisation costs we assume a reading time of 6 minutes per page for Trustees.

[43] 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#contents

[44] 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#contents

[45] 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#contents

[46] https://www.gov.uk/government/consultations/taking-action-on-climate-risk-improving-governance-and-reporting-by-occupational-pension-schemes-response-and-consultation-on-regulations/impact-assessment-on-climate-change-risk-governance-and-disclosure-tcfd-proposals#fn:33

110. We have assumed the regulations will be 2 pages and accompanying guidance will be 35 pages.

Assumptions for system updates

111. We have assumed only "specified schemes" within the scope of the regulations will need to update and test their systems and infrastructure.

112. We have assumed two providers will have lower system update costs as they have already adopted a de minimis. For the other four providers we expect their costs to be higher. This evidence was gathered via the consultation and direct engagement with industry.

Assumptions for communication costs

113. We have assumed only "specified schemes" within the scope of the regulations will need to communicate these changes. It is at the discretion of the provider how they decide to communicate these changes.

114. This evidence was gathered via the consultation and direct engagement with industry. We have assumed providers will only need to directly notify employers and members once.

Assumptions for foregone revenue / member savings

115. Due to commercial sensitivity and availability of data, we have used aggregate figures to outline the number of pots affected and the loss of revenue.

116. To calculate loss of revenue we need to know the number of pots worth £100 or less which are subject to flat fees and the flat fee that is levied. This is commercially sensitive information which will be made available to the Regulatory Policy Committee in an addendum. Where appropriate we have used aggregate figures to outline the number of pots affected the loss of revenue.

117. Our best estimate of the number of pots worth £100 or less that are subject to flat fees is 1.5 million. Using the mid-point of the Pension Policy Institute's[47] estimate that between 20% and 50% of pots may belong to the same member, we have discounted the best estimate of the loss of revenue by 35%. Therefore our best estimate, based on the information provided, of the loss of revenue on these pots is £6.33 million of the loss of revenue on these pots is £6.33 million.

Assumptions for future foregone revenue

118. Our best estimate of the number of pots worth £100 or less over the next 10 years assumes the current level remains stable. Another option would have been to use the Department's Pensions Simulation model, however there are a number of caveats about using this model:

- The model is not designed to model rapid job churn and turnover and we would expect these types of individuals to be responsible for the making of small pots in the future.
- The model looks at individuals rather than providers therefore, we don't know what pension provider the pot is and what kind of charge they would be subject too. Therefore, we have assumed 1 in 4 will be subject to flat fees and the flat fee is around £15, based on what we know about current coverage.
- The model does not account for any changes to national insurance or pension contributions so there may be circumstances where individuals may contribute more or less to their pension.
- These estimates do not account for any future small pots solution.
- The number of pots worth £100 or less modelled for the current year (for the industry as a whole) is a lot lower than the figures provided to us by just the six "specified schemes" who we requested data from, suggesting there is a clear undercount of the very smallest pots.

119. Due to these and the lack of better estimates on how many pots subject to the de minimis there might be in the future, our best assumption is that the current figure of 1.5 million pots stays

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

stable over the ten-year appraisal period. Therefore we estimate the loss of revenue going forward is £6.33 million.

Impact on small and micro businesses

120. The proposed regulations will impact any provider who operate a qualifying scheme used for workplace pensions and who levy a flat fee. This may include small and micro pension businesses although most small businesses do not administer their own pension schemes, but instead use an external provider to meet their duties.

121. The Pensions Regulator[48] found of the 28,360 schemes in the DC landscape, 22,350 (79%) have identified themselves as relevant small scheme (RSS) or an executive pension plan (EPP) with 12 member or less.

122. The government acknowledges that pension scheme members have little or no choice over the scheme they are in, and by including small and micro businesses ensures all members have a degree of protection for their pension savings.

123. Of the 6 schemes we have identified none are small or micro businesses. As reported in the Pension Charges Survey 2020[49] flat fees have become more common in recent years and particularly for larger Master Trusts, therefore it is unlikely that they are used by small or micro businesses.

Wider impacts

Market competition

124. Financial sustainability is a challenge for automatic enrolment providers and delaying paying back their loans may affect Master Trust ability to scale their assets, pursue innovation and prepare for future challenges and regulation.

125. We don’t have evidence on the finances of those who levy a flat fee but they may seek to:

- Re-finance
- Exit the market
- Increase charges on other groups
- Pause other ongoing projects or innovation

In order to cover the loss of revenue from pots of £100 or less. This may put them at a financial disadvantage against providers who do no levy a flat fee and therefore have no financial implications from the de minimis.

Affected member characteristics

126. We do not have data on the characteristics of those with pots of £100 or less who pay flat fees. We have used the Wealth and Assets Survey as a proxy for the types of people who have smaller pension pots. The Wealth and Assets Survey is self-reported; therefore, it relies on accurate reporting of respondents which is not always the case. Some of the data cannot be directly compared with other sources.

127. Analysis of the Wealth and Assets Survey (WAS) found small retained pots (also known as deferred pots) are found in the highest numbers amongst:

- Women (Table 9)
- Lower earners (Table 8)
- Younger individuals (Table 9).

There are caveats to this analysis but we can estimate these groups may benefit the most from the introduction of the de minimis.

48 https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2020-2021

49 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#contents

128. For example, 85% of retained DC pots which belong to those aged 16-24 are worth less than £2500, compared to 26% of retained DC pots belonging to those aged 45-54 and 22% of retained DC pots belonging to those aged 55-64 (Table 9).

129. Moreover, 43% of retained DC pots which belong to individuals with income between £10,000-£19,999.99, are worth less than £2,500. The corresponding figure is 34% of retained DC pots for income group £40,000-£49,999.99 (Table 8).

Member engagement

130. Responses to the Review of the Default Fund Charge Cap and Standardised Cost Disclosure[50] and Permitted charges within Defined Contribution pension schemes[51] consultations suggested the introduction of a de minimis may disincentive members from consolidating their smaller pots as they are at less of a risk of pot erosion.

131. Many members do not make active choices about their workplace pensions. According to the Pensions Regulator[52], around 95% of memberships in DC schemes are invested in the scheme's default strategy. The Pension Policy Institute[53] found this was even higher for members in Master Trust scheme with an estimated 99% in the default strategy.

132. This evidence suggests the majority of members in DC schemes do not make active choices about how their pensions are managed. Therefore, we would not expect the introduction of a de minimis to significantly impact members' decision to consolidate their pots or member engagement.

Monitoring and Evaluation

133. We do not plan, at this stage, to undertake a specific future formal statutory review of the de minimis measure. In view of the interaction of this policy with potential solutions to tackle the proliferation of small pots, and potential future reform of the permitted charging structures, our future policy on the de minimis will be considered in conjunction with detailed proposals in on these wider policy areas.

134. We will consider opportunities to undertake informal evaluation of this measure.

[50] https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure#standardised-cost-disclosure-templates

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

[52] https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2019-2020

[53] https://www.pensionspolicyinstitute.org.uk/media/3590/20200827-ppi-financial-sustainability-of-master-trust-schemes-final.pdf

Annex

Annual Survey of Hours and Earnings

The Annual Survey of Hours and Earnings[54] (ASHE) is conducted by the Office for National Statistics (ONS) and is a key source of information on workplace pensions in GB as it collects information on all types of workplace pension: occupational pension schemes, group personal pensions and group stakeholder pensions.

The survey results are used widely in order to analyse pension participation and to monitor the impacts of pension reforms.

HMRC Real Time Information data

RTI is HMRC's reporting system for income taxed via Pay As You Earn (PAYE). Employers and pension providers are required to report to HMRC payments to employees (or recipients of occupational pensions) on or before each payment date where it is practical to do so. Within RTI, each submission relates to a payment to an employee (or occupational pension recipient) and when they are submitted to HMRC by the PAYE scheme, they are contained within a Full Payment Submission (FPS).

RTI includes information about the PAYE scheme, the employee (or occupational pension recipient), and the payment. However:

- If all employments of one employer are paid less than the Lower Earnings Limit (LEL) (£118 a week or £512 a month in 2019/20) a PAYE scheme is not needed, and the employer is not required to submit RTI. However, if any single employee earns more than this, is in receipt of a pension, has another job, or receives expenses or benefits from the employer, the employer is required to report RTI for all employees[55].
- Employers who are exempt from online payroll reporting do not need to submit RTI electronically. This may be due to religious beliefs, where care services must be provided to the employer or a member of their family, or for other reasons[56].

RTI only holds information on employments and pensions that are reported through the payroll reporting process. RTI does not include information about both Self-Employment and pensions which are not paid via PAYE (e.g. State Pension and income from other sources that is seen as pension income by the individual).

From comparison with the Annual Survey of Hours and Earnings (ASHE), we estimate that RTI covers about 65 per cent of those saving into a workplace pension. ASHE 2018 reports that 35 per cent of employees saving in April 2018 were saving with employer-only contributions or via salary sacrifice.

Wealth and Assets Survey

The Wealth and Assets Survey[57] is a large-scale national longitudinal survey of private households in Great Britain. The survey uses Postcode Address File (PAF) as the sampling frame, and to ensure that the sample is representative of the GB population, 'probability proportional to size' sampling technique is used. Interviews are conducted using Computer Assisted Personal Interviewing (CAPI), and collect detailed information on individual and household wealth in various forms. The analysis presented uses data from Round 6 of the survey which was conducted over a period between April 2016 to March 2018. Overall, 18,400 households were interviewed in Wave 5 of the survey and 16,000 in Round 6.

The data on occupational DC pot size is self-reported and is only based on an individual's two largest occupational DC pots. Therefore, some smaller pots could be missing from the analysis. In addition, as it is self-reported, where an individual has forgotten or "lost" a pension pot they necessarily will not report it and it will not appear in the data.

---

[54] https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/methodologies/annualsurveyofhoursandearningslowpayandannualsurveyofhoursandearningspensionresultsqmi

[55] https://www.gov.uk/paye-for-employers

[56] https://www.gov.uk/guidance/find-out-which-employers-are-exempt-from-online-payroll-reporting

[57] https://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/debt/methodologies/wealthandassetssurveyqmi

Table 5: Percentage of active and deferred pots individuals, aged over 16, reported owning

Number of pots	Percentage
0	61.0%
1	26.7%
2	8.0%
3	2.8%
4	1.0%
5	0.3%
6 or more	0.1%

Note: Frequency and percentages rounded.

Table 6: Distribution of active and deferred pots individuals, aged over 16, reported owning by £100 size band.

Pot size	Percent
Under £100	4.2%
£100-£199	2.5%
£200-£299	3.2%
£300-£399	1.4%
£400-499	1.1%
Over £500	87.5%
Total	100.0%

Note: Percentages rounded. Respondents only asked about their 2 largest active pots and 6 largest deferred pots.

Table 7: Distribution of active and deferred pots individuals, aged over 16, reported owning by £500 size band and gender.

Pot size	Female	Male
Less than £500	14.7%	10.7%
£500-£999	7.5%	5.8%
£1,000-£1,499	9.6%	7.4%
£1,500-£1,999	3.0%	2.6%
£2,000-£2,499	5.5%	4.4%
Over £2,500	59.7%	69.2%
Total	100%	100%

Note: Percentages rounded. Includes only respondents who reported owning a pension. Respondents only asked about their 2 largest active pots and 6 largest deferred pots.

Table 8: Distribution of active and deferred pots individuals, aged over 16, reported owning by £500 size band and income.

Pot size	Less than £10,000	£10,000-£19,999	£20,000-£29,999	£30,000-£39,999	£40,000-£49,999	Over £50,000
Less than £500	5.3%	16.7%	15.2%	14.6%	13.0%	11.8%
£500-£999	3.4%	8.2%	6.3%	8.2%	5.9%	6.5%
£1,000-£1,499	6.5%	10.0%	11.8%	10.1%	8.2%	7.7%
£1,500-£1,999	1.9%	2.4%	3.5%	3.6%	3.2%	2.8%

£2,000-£2,499	4.6%	6.2%	6.3%	4.6%	4.0%	4.7%
Over £2,500	78.3%	56.5%	57.0%	58.9%	65.8%	66.6%
Total	100%	100%	100%	100%	100%	100%

Note: Percentages rounded. Includes only respondents who reported owning a pension. Respondents only asked about their 2 largest active pots and 6 largest deferred pots.

Table 9: Distribution of active and deferred pots individuals, aged over 16, reported owning by £500 size and age band.

Pot size	16-24	25-34	35-44	45-54	55-64
Less than £500	38.8%	20.0%	9.7%	9.4%	8.2%
£500-£999	22.2%	13.9%	4.6%	3.7%	3.4%
£1,000-£1,499	11.1%	12.1%	8.7%	6.8%	6.1%
£1,500-£1,999	5.4%	5.1%	2.2%	2.2%	1.8%
£2,000-£2,499	7.3%	5.7%	6.0%	4.3%	3.0%
Over £2,500	15.1%	43.1%	68.7%	73.6%	77.6%
Total	100%	100%	100%	100%	100%

Note: Percentages rounded. Includes only respondents who reported owning a pension. Respondents only asked about their 2 largest active pots and 6 largest deferred pots.