Department for Work & Pensions

Automatic Transfers

A Framework for Consolidating Pension Saving

February 2015

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Foreword by the Minister of State for Pensions

Major reform of the United Kingdom's pensions system is well under way. Nearly three years ago we saw the introduction of automatic enrolment, bringing more people into pension saving and making pension saving the norm.

In the Command Paper, *Automatic transfers: consolidating pension saving* we set out the issue of the escalation of dormant pots as a result of Automatic Enrolment. With regular job changes in the world of auto-enrolment there is a risk of generating millions of small, stranded pension pots. We took powers in the Pensions Act 2014 to create a 'pot follows member' automatic transfer system, whereby when people change jobs they have the opportunity to consolidate their pension pots into their new employers' pension schemes.

This paper is the culmination of the work that has taken place since the 2014 Act with a wide section of the industry to analyse the different implementation options and drive towards a safe and efficient industry-led model. I am very appreciative of the commitment that those involved in the various working groups have shown in contributing to this work.

Where we can, we have been specific about the features of the new system in this paper - especially around the technical aspects of communications and the phased approach. My goal is for the initial phase of automatic pot-matching to be in place by Autumn 2016. I know there is still work to be done to make this happen. I look forward to continue working closely with the industry as the model develops.

Steve Webb MP

Minister of State for Pensions

Chapter 1: Introduction

1. The successful rollout of automatic enrolment is transforming the pension landscape. Over 5 million people have already been automatically enrolled into a workplace pension scheme, and this will increase as small and micro employers are brought into automatic enrolment over the next 3 years.

2. This is a great success and one that is welcomed by government, regulators and the pensions industry. More new pension savers, the majority saving into money purchase schemes, means there will be a significant increase in the number of small, dormant pension pots throughout the pensions system. Our analysis has shown if we do not take action there will be over 50 million dormant pots by 2050.

3. Our analysis also highlights in many cases it is inefficient for pension providers to administer small dormant pots, and the breakeven level where a small pot becomes profitable varies between schemes. It is therefore in the interests of pension schemes that a solution to the problem of multiple small pots is found. We intend to provide a legislative framework that allows the industry to solve this problem efficiently and innovatively.

4. Members' interests are not best served by multiple small pension pots scattered between pension providers because of the increased risk in losing track of one or more pots. We therefore want to introduce a system that consolidates these small pots and helps individuals keep track of their pension savings as they move between employers. We believe the consolidation of pots will also help build engagement with pension saving and the industry will be more efficient with fewer dormant pots because of their associated costs.

5. To address this problem the government introduced a legislative framework to enable pension pots to follow members as they move employment in the Pensions Act 2014. This will see the automatic consolidation of members' small pots into the workplace scheme they are actively saving in. These legislative powers set out a number of key features in the design of an automatic transfers system where the pension pot will effectively follow the member into their new pension scheme:

   - The system will be facilitated by pension schemes, rather than by employers.
   - Eligible pots below the pot size limit, built up in the money purchase default arrangement of workplace schemes will be automatically transferred.

Members will be provided with information about the transfer and will have the ability to opt-out where they want to keep their pension pot with their current scheme.

6. Pension provision in the United Kingdom is diverse, with schemes of varying size and complexity being delivered under different legal frameworks and regulated by different bodies. Any system where a pension pot is automatically transferred needs to be sensitive to these differences and work throughout the pension landscape. There are complexities in relation to the guarantees and features that are associated with some pension pots, as well as the implications of tacit member consent. Feedback from our working groups indicated that any attempt at a voluntary industry solution to introduce a system of this scale would be unlikely to succeed. In addition diversity in the market means a one-fits-all solution would not be sensible and therefore, by allowing the industry to implement this change through what we call a federated model of registers, we would drive efficiency taking into account the variety of schemes that will be involved in automatically transferring pension pots.

7. We have approached the policy mindful of these issues and have set up this project in a way that best addresses these challenges directly. We have worked closely with the industry from the outset and believe any solution must be industry led with the government providing a legislative framework only where necessary to enable an effective solution. This has challenged our assumptions and brought about a change on some policy areas - the most notable of these changes was the move from a centralised database to a federated database. However, we are mindful that this marks a departure from our original proposal; further work will take place to ensure this new model aligns with our legislative powers under Schedule 17 of the Pensions Act 2014 prior to implementation[1].

8. It should be highlighted that in this document we discuss schemes and registers as separate entities. This is for clarity only and when the term register is used this is to separate the additional functionality that schemes must be able to perform to automatically transfer pension pots. Some registers will be owned by schemes and some registers will be third parties contracted by schemes to fulfil their regulatory obligations to automatically transfer pension pots. We hope that by differentiating scheme functions from register functions it is useful for those parties who are considering what they must do to provide this register functionality either in house or as a third party supplier.

9. We have chosen to implement the system of automatically transferring pension pots on a phased basis as outlined in chapter 5 of this paper. Phase 1 will limit the number of schemes making automatic transfers and will see the use of a

[1] http://www.legislation.gov.uk/ukpga/2014/19/schedule/17

member opt-in process for pension transfers to take place. Phase 2 will move towards full rollout in terms of scheme coverage and utilise an opt-out member communication where transfer will take place in the absence of member choice. We believe this phased approach will enable us to assess the practical implications of the system and test its success. We remain committed to implementing an automatic solution to the increasing number of small dormant pension pots even when the individual is fully disengaged from their pension saving.

10. Questions remain in some areas such as identity verification of the individual by pension schemes, or how best to ensure communication interoperability of registers. We will continue to work with industry to come up with innovative answers where there is no definitive solution.

This Paper

11. This document sets out how we expect to implement a system of automatically transferring pension pots. It references the decisions we have taken so far, and it confirms our intention to introduce this system from October 2016. It also outlines our phased approach to implementation which will allow the model to be tested ahead of full roll-out.

12. The rest of this paper describes our preferred implementation model. We describe this as the ‘federated model’, which will see a network of registers that store and match information about eligible small pots. This will require schemes to match data in a standardised way. Whether they choose to do this on their own platforms or contract with third parties to provide this functionality is a decision schemes can make on an individual and commercial basis. As such throughout this paper the term register relates to this functionality, irrespective of whether it is provided directly as a scheme function or if this is a third party contracted to perform these functions on behalf of schemes. As we expect a mixed ecosystem of in house and contracted out registers to evolve, we feel it is clearer to outline the new functions in this way. Annex A sets out the technical standards we think these registers should meet.

13. After introducing the federated model, the chapters following this describe the key stages of operation for a pension pot to follow the member. This includes details of the phased approach of implementation and the types of schemes and benefits that will be eligible to be automatically transferred. A step by step description of the actions schemes will take to process pension pot information is also included at Annex B of this paper.

14. The Pensions Act 2014 received Royal Assent on 14 May 2014 and since then we have been working closely with a large number of stakeholders. We have included a list of the groups we have worked with throughout this period at Annex C and we are extremely grateful to the many individuals and organisations who have generously given their time and expertise to shape this work.

15. Taken together we hope this paper and annexes provide a thorough explanation of our intentions for implementation. We believe this will be particularly useful to pension schemes considering what changes they may need to make ahead of implementation in October 2016.

Next Steps

16. Our next step is to develop the legislation for the federated model of automatically transferring pension pots from October 2016. It is not our intention to regulate for every detail set out in this document but rather to create an appropriate legislative framework for schemes to operate within. We are keen to ensure innovation and future development is possible within the industry, and the selection of the federated model was chosen to encourage this. We will therefore look to legislate in such a way that compliments that approach and balances regulation with the flexibility to innovate.

17. The Pensions Act 2014 includes powers for the Secretary of State to create a compliance regime. The scope of the project means many regulatory bodies may have links to an automatic transfers system, such as The Pensions Regulator, the Financial Conduct Authority and the newly created Payment Systems Regulator. To consider the next steps in isolation of these factors would not provide the joined up approach necessary for successful implementation.

18. We will continue working with the industry in our working groups and all other interested parties and we will confirm our approach as early as possible. We expect this to be in advance of consulting on the draft legislation to implement this system later in 2015.

Chapter 2: The Federated Model

1. Our preferred approach to implementation is what we call a federated model. This is a network of interoperable registers which will hold information about pension pots eligible to be automatically transferred. This network of registers will be used by pension schemes to match information about pots eligible to be automatically transferred across the industry.

2. This model is a result of work undertaken with a stakeholder working group in 2014 to evaluate different implementation models. Since this initial recommendation we have been working with a wide number of stakeholders to further develop the details about how the federated model will operate.

3. This chapter sets out the background to our decision to develop the federated model and information about how the register functionality will operate. Further information about the standards that are to be met for this are contained within Annex A.

Background to the Federated Model

4. Significant work has been undertaken in the last year. The Bill that became the Pensions Act 2014 gained Royal Assent in May 2014 and provided the enabling powers for a system of automatically transferring small pots. We then began working with a group of representatives of the pensions industry, IT providers and regulators to assess different implementation models. The options assessed by this group included:
   - A paper-based system where members would be given a Pensions Transfer Identification Document when they left one employer’s scheme, to hand to their next employer.
   - A single, centralised register holding information about all pots eligible for transfer.
   - A network of smaller, interoperable registers holding information about all pots eligible for transfer.
   - Utilising existing HMRC dataflow to identify pots eligible for transfer.

5. The group recommended that the first and last of these options were not suitable implementation options – the first because it relies on manual processes and is

not automatic, and the last because existing HMRC dataflow does not provide the information necessary to make automatic transfers work, and the cost of developing that to facilitate a system of automatic transfer would likely be prohibitive.

6. More time was spent assessing the benefits of a single or centralised register of pension pot information and a network of smaller registers. The working group recommended to DWP that – while either model could be a successful implementation option – the federated model was preferable.

7. While a centralised register would require all schemes to communicate with a single register, the federated model reduces concerns over a single point of failure and a single point of data storage. It also allows for registers to operate in different ways according to the different needs of sections of the pension market. For example, one register might accept data from schemes in a manual format, while another may only accept data sent by electronic messaging. Without these registers schemes may have to communicate to all other schemes directly in order to match pension pots.

8. Competitive forces should ensure they stay up to date over time. In contrast there were concerns that a single register – whether provided by government or by the pensions industry – may not keep up to date with technological advances and industry innovation to the same extent.

Register Functionality

9. All schemes that must automatically transfer pension pots will have to identify and flag data of pots eligible to be transferred. Schemes will then ensure this data is held on a register in order for these pension pots to be matched and automatically transferred. They must also be able to search for flagged pots held by other schemes. Schemes may choose to develop this register infrastructure in house or they may choose to contract with third parties to fulfil their obligations to perform these functions.

10. We are working with industry groups to ensure efficiencies are realised where possible. As a result the register-to-register interaction will be standardised which will allow “straight through processing” of messages. It is fundamental to the success of the federated model that the network of registers is interoperable. This means that every register in the network is able to communicate information with all other registers in the network. Without this some pension pots would not be matched and the coverage of the system would be incomplete.

11. Where schemes contract with third parties to provide their register service, they will also be able to contract in relation to how they wish to communicate information to their registry provider. This balances the varying requirements of schemes with an efficient and cost effective solution. This will also ensure the costs of inefficiencies at scheme level are borne by the inefficient party and not forced onto other schemes. Those schemes unable to make a business case for upgrading their systems from a manual to more automated process will contract with their registers to perform this automation. The receiving scheme will have no additional burden processing bespoke information manually, as the registers will standardise the information in order to match pots.

12. In order for this to happen effectively the registers will be required to meet a defined set of Open Standards around how they hold, send, and deal with data. These standards will be published to ensure it is clear what is required. Schemes will then be responsible for ensuring that the register they select offer compliant services.

13. These published and freely available Open Standards will also serve to ensure there is a transparent route to market for schemes and prospective third party registers. A specialist stakeholder working group has advised us on what standards would be appropriate to ensure a secure, efficient and interoperable network. The conclusions of this work are set out at Annex A.

14. This is in keeping with government policy on Open Standards. By implementing the Open Standards Principles for software interoperability, data and document formats, government bodies are supporting the delivery of:
    a. A level playing field for open source and proprietary software providers competing for IT contracts.
    b. Improved flexibility and ability to cooperate with other bodies, individuals and businesses.
    c. More sustainable cost in IT projects.
    d. Transparency in specification and implementation requirements.

15. Automatically transferring pension pots will increase the number of pension transfers taking place. Given the limited size of the pension pots being transferred under this system high transfer costs could erode pot value and operate counter to the policy intent. As such we are exploring how to reduce the cost of pension transfers. Analysis and feedback from the industry has given us an estimated cost of a pension transfer and a breakdown of how these costs are apportioned – although this will vary from scheme to scheme and depending on the details of the particular transfer.

16. The costs involved in transferring a pension pot automatically are difficult to estimate at this stage given this is a new process. There are processes for member initiated transfers that we intend to remove which will make the process automated, and as such administrative costs for each transfer should reduce.

17. From data we have received from the industry a significant proportion of cost in any pension transfer is employee time in processing the transfer and performing due diligence on the intended receiving scheme. In Phase 1 we can minimise or eliminate this cost by setting up a defined list of schemes that will be included within the system and in order to automatically transfer a pension pot both the ceding and receiving scheme must be on this list. A transfer can then be made without the per-transaction due diligence previously required. Statutory discharge will be given to schemes where such a transfer is made in a compliant manner.

18. Those included on the list in Phase 1 will be chosen by their size and number of members. This means schemes and administrators that provide pension pots for the largest number of members and cover the majority of the market will be included. The justification for this is based on analysis both within our working groups and in liaison with outside agencies. In the absence of any objective qualitative criteria we feel this is a sensible approach.

19. This list will be assessed moving to Phase 2 of implementation if qualitative criteria can be established allowing for an objective assessment of eligible schemes.

20. The wider and long term costs of the system are addressed in our impact assessment that was published in 2012[2]. This highlights the long term savings to industry in the analysis. When we consult on regulations later in the year we will publish an updated impact assessment with revised figures as we understand more the scope of the system and the associated costs.

21. Further cost reductions are anticipated in the standardised message formats that lend themselves to automatic processing of queries. We also believe that payments should be electronic – rather than cheque based, as cheque transfers can push cost onto the receiving party. We are investigating how we can implement this with minimum impact.

[2] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/184965/small-pots-automatic-transfers-impact-assessment.pdf

Chapter 3: Automatic Transfer Schemes

1. We previously announced that pension pots will automatically follow the member only between ‘pure’ money purchase benefits. We also intend to make a limited number of other exceptions where it may not be in members’ interests to be transferred out of particular types of arrangements.

2. There are two principles behind these exemptions. The first is that automatically transferring pension pots should be targeted on those individuals who are least likely to be actively engaged with their pension savings. The second is to ensure that members are only transferred into default arrangements. These arrangements are defined by The Occupational Pension Schemes (Charges and Governance) Regulations 2015[3] (‘the Charges and Governance Regulations’) that, subject to parliamentary approval, will come into force from April 2015.

3. Following these principles, there are some types of scheme that we do not think it would be appropriate for individuals to be automatically transferred out of or in to:
   - Relevant small schemes, with fewer than 12 members where all of these members are trustees, and either the rules of the scheme provide that all decisions are made only by the trustees who are members of the scheme and by unanimous agreement; or the schemes has an independent trustee and that trustee is registered on the Pension Regulator’s register of trustees.
   - Executive pension schemes, where a company is both the only employer in relation to the scheme and the sole trustee, and the members of the scheme are either current or former directors of that company and include at least one-third of the current directors.
   - Schemes with only one member.

4. In each of these cases, members are effectively governing savings on their own behalf and can therefore be expected to be engaged with their pension savings to the extent that it would not be appropriate to automatically transfer them into or out of these investments.

5. Within all other workplace schemes, we propose that transfers should take place where the member is saving into a charge-capped default arrangement, as defined in the Charges and Governance Regulations in both the ceding and receiving scheme. While this slightly adds to the pot-eligibility criteria, we think it is

[3] http://www.legislation.gov.uk/ukdsi/2015/9780111128329

an important safeguard of members' interests both in avoiding transferring funds where the member has made an active decision about investing these outside of the default, and in ensuring that members will only be automatically transferred into low-charging funds. This will exclude all additional voluntary contributions from automatically transferring except where these are into a fund which is designated as a default arrangement for another employee of the member's employer.

6. This safeguards the member and ensures the fund they are to be automatically invested in will be a charge capped fund of a standard suitable for automatic enrolment.

7. It has been highlighted that in some circumstances where the member has a pot invested in the default fund it is possible for a proportion of this member's investment to be to be invested elsewhere following an active decision by the member. Some schemes may have to identify pots that have these features and this may be an additional expense for this check to take place. Where the member has actively chosen an investment strategy it has been highlighted that automatically transferring their funds following this may not be in their best interests. We believe in Phase 1 the opt-in communication addresses the issue of member choice as they will be given the option to actively choose at this juncture and in the absence of a decision their original choice will remain valid.

8. When we move to Phase 2 and the member opt-out communication we acknowledge we need to investigate the implications around default funds and member choice further. This must be considered in tandem with the industry and with a view to the details of the communication the member receives.

9. Tests for identifying those funds that are required to meet the charge cap are set out in the Charges and Governance Regulations. Schemes will already be required to assess their funds against these tests in order to ensure compliance with the charge cap regulations. We therefore hope that any additional work required in order to determine whether a member is saving into a charge-capped fund for the purpose of determining automatic transfer eligibility will be very limited.

Chapter 4: Key Stages

1. This chapter describes four key stages in the operation of automatically transferring a pension pot – pot flagging; pot matching; contacting the member; and pot transfer. It further touches on the timescales of operation for many of these stages. Further detail on each of these stages can be found in the step by step guide for schemes to understand the operation of the federated model contained in Annex B.

Pot Flagging

2. This system will target the transfer of small pension pots built up since the introduction of automatic enrolment. This is intended to focus on those individuals least likely to have engaged with their pension savings as well as those schemes that are more likely to be administered on more modern platforms.

3. Pots will therefore be eligible for transfer if they meet all of the following criteria:
   - The first contributions were received on or after July 2012, to coincide with the beginning of automatic enrolment.
   - The pot is worth £10,000 or less at the point of valuation. However, provisions in the Pensions Act 2014 ensure that the Secretary of State will review the pot size limit every 5 years.[4]
   - The pot is invested in a charge-capped default arrangement at the point of valuation.

4. Schemes will be required to assess pots against these criteria when they become aware that the member has stopped contributing to the scheme (further information about when schemes are deemed to be aware of this is contained in Annex B). Funds fluctuate regularly and this will also be the case after the point of initial valuation. We recognise this means in some cases pots may transfer although they have increased above the £10,000 limit since the point of valuation. Conversely pots once valued above the limit will not be transferred even if their value drops below this level after valuation.

5. We expect these cases to be uncommon and from analysis we have seen, occurrences of dormant pots that have risen above the initial limit are rare at 5% of cases. This will depend on the value of the initial fund, with those closer to £10,000 at the point of valuation more likely to increase over the threshold. The

[4] Pensions Act 2014, Schedule 17, paragraph 13

incidence of pots valued above £10,000 falling below this is much lower at approximately 0.5% due to market trends. We expect in the early years of implementation flagged pots will be small because of the first contribution date criteria which coincides with the beginning of automatic enrolment in July 2012. We have considered the possible benefits of introducing a second stage of checks against the eligibility criteria and we do not think these are appropriate given the additional cost and the relative risk involved. Limiting the eligibility of pots to those invested in default funds may also reduce these occurrences.

6. Where schemes identify that a member has left a scheme and has an eligible dormant pot they will communicate information about this pot onto their chosen register. As set out above, schemes can choose whether to contract with a third party register, or whether to build this capability themselves in house. In either scenario it is important that all schemes record the same pieces of information about eligible pots in order that these can then be matched to the member when they move to another scheme in the future.

7. Our stakeholder working group has helped to determine what these data items should be. In order to help ensure the efficiency and cost effectiveness of the system we have focussed on identifying the fewest pieces of information which can be used for effective pot matching and member communications that bears in mind what information should already be held by schemes.

8. The following pieces of information will therefore be required to record pots eligible to be automatically transferred on a scheme's register:
   - First initial and surname.
   - Date of birth.
   - Gender.
   - National insurance number.
   - Employer that pension pot was accumulated with.
   - Pension scheme tax identifier number.
   - Pot identifier or reference number.

9. The Pension Regulator's record keeping guidance notes that a National Insurance Number is one of the eleven common data items they expect schemes to hold.[5] This is an area that we will return to if it becomes apparent that inclusion of the National Insurance Number is negatively impacting the effectiveness of automatically transferring pension pots. Other common data items also included in the guidance are surname, initials, gender, and date of birth.

[5] TPR guidance on Record Keeping, published June 2010, available at http://www.thepensionsregulator.gov.uk/guidance/guidance-record-keeping.aspx#s1676

10. Additional data items we expect schemes to have are those that identify the pot within their own systems, such as a reference number that may be unique to that provider and the employer that the contributions relate to. Our communication working group highlighted that this information may be important for the member to understand what pension pot a particular communication relates to.

Pot Matching

11. When a new member joins a workplace pension scheme, that scheme will search for eligible pots associated with the member which have been flagged by previous schemes. The mechanism for doing this under a federated model will be to instruct the scheme's register to search for flagged pots that match the key criteria about the member.

12. In considering the criteria for pot-matching there is a balance to be struck between generating the maximum number of positive matches and avoiding any erroneous matches. While we want to see as many automatic transfer matches as possible, we have prioritised reducing the risk of erroneous matches.

13. A positive match will be made if a pot is found on a register that matches the following pieces of information:
    - Date of birth.
    - National Insurance Number.
    - At least two from:
        - Initial.
        - Surname.
        - Gender.

14. Only exact matches of these data items will be deemed to be positive matches. We believe this list strikes the right balance in generating a high number of legitimate pot matches while avoiding false partial matches. However, the effectiveness of the pot matching criteria is an area we will be particularly interested in monitoring in the first phase of implementation.

Contacting the Member

15. If the pot matching exercise produces a positive result, the scheme that initiated the search will contact the member to let them know that matched pots have been found for them. Where no matched pots have been found, there is no requirement for either scheme to contact the member to let them know this.

16. We have taken note of the lessons learned from automatic enrolment in considering the communication requirements for automatic transfers. In particular focussing on key messages, and providing information in clear, accessible language is crucial. We also want to ensure that messages about automatic transfers do not interfere with communications about automatic enrolment, and vice versa.

17. A stakeholder working group has advised us on communication requirements throughout the member journey. In general, we have tried to build on existing communication points, rather than introduce new contact points into the member journey. The exception to this is the new contact point ahead of a pension pot being automatically transferred.

18. In the first phase of implementation, this communication will be used to ask the member whether they would like the transfer to go ahead (opt-in). Once automatic transfers is fully operational, this will change so that the member is informed that the transfer will take place unless the member chooses to cancel it (opt-out). More information about this phased approach to implementation is included in Chapter 5.

19. An opt-in member communication may have different or additional implications to those of an opt-out communication. It is our intention that the communication will not constitute regulated advice to the member but should provide enough information to be of use to the member in making a decision on whether to opt-in to the transfer or not. We intend to work with the regulator and stakeholder groups to ensure that the member communication is appropriately defined within these limits.

20. This communication will need to include some key messages and pieces of information to ensure the member is given sufficient information to understand their options. While some differences will be needed between the communications to members between the initial opt-in phase, and the opt-out phase, there are key pieces of information that are common to both:

    a. **Short, clear explanation of automatic transfers:** the notification should include a short, clear description of the process of automatically transferring pension pots, including assurance that this is a legislative requirement.
    b. **Options and next steps:** the member needs clarity about what options they have to take action.
        i. **Phase 1 Opt-in:** this communication will highlight how to approve the transfer and whom to contact to do so, as well as the timescales within which to do this.

   ii. **Phase 2 Opt-out**: this communication will outline the implications of not responding – that the transfer will take place unless the member responds. It must also include timescales within which a response should be received to halt the transfer and both how and to whom they give this response.

c. **Information about their previous pot(s):** while information on previous pots need not be extensive, it needs to be sufficient for the member to identify these pots as theirs and understand enough to assess the implications of transfer. The notification should therefore include the name of their previous pension provider and employer they were saving through.
d. **Policy or account numbers:** numbers of the savers current and previous pots are needed to ensure efficient communications with schemes

21. Identity verification of the individual before automatically transferring their pension pot has been highlighted to us as an important step and we appreciate we must assess the risk, cost, and responsibility for fraud in this area. We maintain that the value limit for automatic transfers, the employer link, and the identity checks that are required on pension withdrawal mean by automatically transferring pensions we will not substantially increase the risk of pension scams. We are looking at different avenues to reduce this risk as far as practicable, such as audit trail requirements, member communications and requiring the individual to provide evidence of their identity prior to automatically transferring their pension.

22. How to balance the cost of additional identity checks against the risk inherent in the system must be investigated. This is made particularly challenging as the greater the involvement we demand from the member in the process the less likely a disengaged member will complete the steps to allow a transfer to take place. This may prevent members transferring in instances where it is in their best interests to do so.

Pot Transfer

23. Once pots have been matched, and the member has had the opportunity to confirm the transfer, the receiving scheme will contact the ceding scheme to request transfer of the member’s pot.

24. There are already a number of money-transfer mechanisms that schemes use to securely transfer funds between themselves, including BACS, CHAPS and Faster Payments and we do not propose to intervene to require schemes to transfer funds by a particular mechanism. We do however think it important that transfers are made in a way that is efficient and cost-effective for both the ceding and receiving scheme. We think payments relating to automatically transferred pots

should be by electronic means. Payments made by cheque, because of the manual processing costs they entail, can push cost to the receiving scheme. More work is required to define the limits of this and how this will be implemented.

25. The technical working group have considered how far payments for multiple pension pots could be combined into a single payment and throughout our work we have been conscious not to exclude the possibility of one payment for multiple transfers and the potential cost savings this may have. As such the technical working group has investigated solutions that include details of how this can be done in a standardised way to realise these benefits efficiently. This necessitates creating requirements where a single payment can be untangled through the use of a reference number that relates the details and values of all the individual pension pots within that payment. This will allow for accurate payment reconciliation by the receiving scheme when these types of payments are sent without incurring the costs of additional staff time in manually processing these. If the ceding scheme choses to send payments in this way the receiving scheme must, provided they are properly formatted, accept this.

26. Consideration of the time limits that transfers must be made within is essential for the benefits of such transfers to be realised. If a transfer must take place within two days there is no scope to bulk payments from an entire week and still comply with these limits. We must balance these competing interests and intend to investigate this in more detail.

27. Payment netting was also discussed in working groups as a potential efficiency, whereby parties offset their incoming and outgoing transfers between each other and only send or receive the difference in value between these transfers. This may be done by parties on bilateral agreements if this is seen as beneficial. However, it is not something that will be required functionality for the implementation of automatically transferring pension pots.

28. Some registers may offer services to help schemes manage transfer payments, for example in providing information to help schemes reconcile these payments or facilitating the transfer on their behalf. We see this as an added value service that schemes and registers may choose to offer on a commercial and individual basis.

Timescales

29. At points throughout the process of automatically transferring a pension pot there are activities which need to take place within particular timescales.

30. The diversity of the workforce means some people take career breaks and parental leave, or have time between jobs. Even when an individual leaves an

employer and begins a new job the next day there can be a delay in consolidating the pension pot. This is to ensure that pots are only flagged as eligible for transfer where there is a high degree of certainty that the member has stopped contributing to that pot. The final position we have decided upon is that where a member has not contributed to the pot in the twelve months following the last annual statement that pot can be deemed eligible for transfer. This means that a period of almost two years can elapse between actual cessation and before eligibility of a pot to be automatically transferred arises as in this example:

a. Member makes last contribution 31st January 2012.
b. Annual statement is sent out on 31st December 2012.
    i. A contribution having been made within the preceding 12 months means the eligibility criteria is not satisfied.
c. Pot is eligible for transfer on 31st December 2013.
    i. As no contributions have been received in the 12 months prior to the annual benefit statement the pot is now eligible to be automatically transferred.

31. This ensures pension pots are not flagged as dormant when contributions have temporarily ceased as may be the case when a member is on a zero hour contract, or where the member works for two or more employers on a rotating or seasonal basis. As such much of the pot matching phase is not designed to operate at a fast pace. We have decided it is sensible to ensure pots are only flagged when they are truly dormant rather than have the potential for pots to be transferred between schemes when this would be disadvantageous to the member.

32. However, at the point of transfer we feel time is critical because we want to minimise out of market risk. When the ceding scheme disinvests the pension pot in anticipation of transferring there is a risk the member will be disadvantaged if the market increases before the funds are reinvested in the receiving scheme. As such we must ensure that once disinvestment takes place the transfer is completed in good time to protect the member from losing out.

33. Member-initiated pension transfers take a varying amount of time from days to several months. Some services have been developed to resolve this delay and reduce transfer times. While progress is being made in driving more efficient member initiated transfers, we think the automated nature of transfers in this system means we can be ambitious with the maximum period a transfer should take place within, and we think these transfers should take place within a matter of days not months.

34. To assess the timescales and the success of pot matching and pot transfer we anticipate there will be a need for crucial management information. This will be

the case in all phases of the system. We intend to assess these further and define them in detail in the next stage of our work.

Chapter 5: A Phased Approach to Implementation

1. We want to ensure as many workplace pension schemes offering money purchase benefits as possible can automatically transfer pension pots, and our work with stakeholders has been focussed on the design of a system that can be rolled out to cover the whole market.

2. However, we recognise that the introduction of a new system of this magnitude needs careful handling, in particular to minimise the impact of any teething difficulties that may arise in the early phases of implementation. We therefore intend to take a phased approach to the introduction of automatically transferring pension pots to allow for the testing and development of the infrastructure ahead of full roll out. We propose two distinct phases.

Phase 1

3. The first phase of implementation will provide high, but not 100% market coverage. A limited number of schemes will take part in this phase so that the initial implementation is contained to a practical number of providers to test the infrastructure with and get feedback from.

4. The consolidated nature of the market for workplace pensions means that a high degree of market coverage can be achieved by including a relatively small number of pension providers. Data we have received from The Pensions Regulator outlines market coverage in terms of membership (i.e. number of members). These figures show that the 20 largest administrators cover 94.5% of members for all third party administrators. Including both third party and in house administration means the 20 largest administrators cover 73% of members. We expect the market to consolidate further in the future as automatic enrolment is rolled out.

5. We have considered restricting initial implementation to a very small number of providers – for example, 2 or 3 – and increasing coverage from this starting point. However, we do not want to create divisions within the market where providers who are otherwise competing for business would find themselves treated differently where some may automatically transfer pension pots and others are unable to do so.

6. It is therefore our intention to set the initial participants so that the majority of members in the automatic enrolment market will be included. We recognise that the industry needs a clear indication of who is going to be involved in the system in advance. We will provide further information on who is included in in advance of when we consult on regulations later this year.

7. There will be a statutory discharge for schemes, and when the conditions of automatic transfers are met, a transfer must take place. This is necessary for an automated system to operate. In the first instance this list will be based on the size of the trust, provider, or third party administrator but work remains to be done to define the compilation of this list. Size is an appropriate proxy as we can balance the market coverage while keeping the initial number of participants at a manageable level.

8. As the ability to automatically transfer pension pots will be rolled out over time to all workplace schemes insofar as they offer money purchase benefit, it will be important that schemes start recording information about dormant pots that are eligible to be automatically transferred on their systems, regardless of whether their scheme has yet been brought into system.

9. Phase 1 will also see members contacted to confirm whether they would like their matched pots to be transferred, before the transfer takes place. Pot flagging and pot matching will be undertaken in the same way as under an opt-out model of automatic transfers. However, the opt-in approach will provide an additional safeguard for members in the initial phases of operation by only transferring their pension pots when they choose that action, as well as restricting the number of transfers that actually take place while the implementation of the new flagging and matching regimes is being tested.

10. Where members confirm that they would like the transfer to go ahead, the transfer will take place, subject to any necessary identity checks to verify the individual if required. Where the member does not confirm that they would like the transfer to take place, no further action will be taken. When the member next moves employers, their eligible dormant pots will be matched again and they will have another opportunity to opt-in to the transfer.

11. Phase 1 will be used to test the initial operation of the automatic pot flagging and matching infrastructure. When this phase is completed we will move to Phase 2, which will transition from an opt-in to opt-out model. We will analyse any changes necessary and move onto Phase 2 as soon as is practicable.

Phase 2

12. In this second phase, the search for eligible dormant pots will take place automatically and the member will still be contacted about any matched dormant pots. However, rather than contacting the member to confirm the transfer of funds, the member will be told that the transfer will happen automatically unless they choose to cancel it. This will be a switch from opt-in to opt-out communication with the member, where the default position will be to transfer a pension pot in the absence of a member response.

13. The industry's experience of members' engagement with pensions suggests there will be a significant difference in the number of transfers that take place under an opt-in and opt-out model of automatic transfers. We therefore want to ensure that the efficiency, accuracy and security of the implementation is fully tested before we move to Phase 2.

14. At this point we will also decide whether a greater number of schemes and providers should be brought into automatic transfers at the same time as moving from the opt-in to opt-out model, or whether this expansion in coverage should take place at a later stage after the opt-out model has been established.

15. We will continue to investigate the use of qualitative criteria to define the list of schemes included in automatically transferring pensions. When we feel we can define criteria that is effective we would then move to this as a basis of those included in automatic transfers.

Further Phases

16. Further phases could be used to extend the scope of pension pots automatically following members. While we anticipate that the first two phases will provide sufficient coverage to satisfy the policy intent, further improvement and expansion of the system will not be ignored. As schemes move onto more modern platforms data clarity may increase and in the future through data cleansing or greater understanding of the matching process the scope could be expanded. As such some further phases are explored below:

    - *Expansion beyond default funds* - we would not wish to regularly change the scope of funds eligible for automatic transfers and consideration would need to be given to any potential implications on industry as they will have the burden of flagging all default funds, and then going back and flagging funds that meet the new criterion.

- *100% of market coverage* - there are considerations that make this difficult in the current pensions market, such as how to ensure receiving schemes are not pension scams on an automatic basis. For example, confirming whether a new scheme is a genuine pension scheme without incurring the increased transfer costs around due diligence.

- *Expansion of pot eligibility* - pot eligibility may be expanded on a number of criteria; for example beyond money purchase benefits or pots created prior to 2012 could be included. There are questions around data quality and how to ensure effective pot matches for these older pots. Further issues arise with many of these pots as the potential guarantees and other benefits or restrictions mean it is very difficult to put them in scope without detriment to the member. However, we feel this should be assessed on an on-going basis.

- *Integration into a pension dashboard* – this may be feasible in the future as the registers could be expanded to provide dashboard information. This would be particularly useful if the system has expanded in scope to include a broader range of pot types and dates of their creation. This would not have to be pots that are available for transfer, but information provided by the scheme for the specific purpose of pension dashboard collation.

17. We would like to thank all the stakeholders we have worked with over the past year. Their work and feedback has been instrumental in helping us shape how automatically transferring pension pots will work. We look forward to working further with these stakeholders as we define the remaining details of an effective and efficient system that works for both individuals and pension schemes.

Annex A: Standards for Register Functionality

1. As outlined in the main body of the paper, we have decided to pursue the federated model to automatically match and transfer pension pots, where schemes are required to store and communicate details of eligible dormant pension pots on a register.

2. In this model, all registers need to be interoperable – i.e. a new match request coming into one register from one scheme will need to be sent to all other registers as it will not be known where any dormant pots may be held.

3. We have been working with our technical group comprising specialist stakeholders to look at how this interoperability will be achieved, based on:

    a) defining standardised data items, formats and matching messages
    b) setting the minimum standards required for communication networks, access and security.

4. Our intention is to provide sufficient legislation to ensure the secure and effective recording, matching and transfer of eligible pension pots. Above this we expect pension scheme providers and their IT partners to develop services that best meet their needs and the needs of their members.

5. We believe the operation of the registers should be conducted, as much as is possible and practical, using Open Standards. This should ensure the continued flexibility, competition and innovation of the registers.

6. Working with our expert stakeholder group, we have identified the key elements of the technical implementation:

    a) Pot matching – the data standards, messages and governance required to hold and match pension pots.
    b) Pot transfer – the data standards, messages and governance required to initiate pot transfer.
    c) Register interoperability – the choice of network, connection protocols, security features and processes by which matching and transfer messages will be relayed.
    d) Network governance – oversight and continuous improvement of the matching and transfer process, including dispute resolution between registers.

7. There are different options under each of these elements, some of which imply how the rest of the approach would look whereas others are independent. For example, pot matching standards could be developed and employed across almost any network, whereas the choice of network may dictate the governance and security arrangements for that network.

8. To help give focus to the options analysis, four implementation proposals were put forward. There are positives and negatives for each of these options that the technical group explored in detail:

    a) Use existing standards and networks – i.e. ISO20022[6] messaging standards over a value added network. Registers would still have flexibility to use other networks that met agreed standards.
    b) Create new standards and define a network based on open architecture and protocols. Messaging standards would be bespoke to automatic transfers and registers would have flexibility to use other networks that met agreed standards.
    c) Use ISO20022 messaging but allow registers to use a network of their choice (subject to it meeting agreed standards), connecting different networks via a 'routing hub' in the middle.
    d) Use ISO20022 standards but do not specify a default communication method. Registers are required to work with each other to agree how best to interoperate (such as each supporting a small range of agreed networks, or using a broker to transfer messages across different networks).

Outcomes

9. In all scenarios considered it was felt where parties agree they may use any network that meets minimum security criteria in order to allow diversity and innovation. The default network is a network that must be used where there is no agreement to use another network for register-to-register communications.

10. The majority of the group agreed that a default network should be defined and this is a key step towards ensuring interoperability. Objectively assessing the network options led to an impasse between a value added and web based network as the two preferred solutions. The group thought that an existing value

[6] ISO20022 is a catalogue of messages that are extensively used in the financial industry and where a new form of messages could be created within this framework for the purpose of automatically transferring pension pots. See http://www.iso20022.org/ for more details.

added network should be defined given the timescales involved, but both solutions were deemed workable by the group in principle.

11. Whilst stakeholders would like a default network to be defined by DWP, we would prefer that the industry agrees its own solution, based on the minimum standards set out.

12. If no such agreement can be reached then we believe the only viable option is for us to define a web based default network. We acknowledge this option does bring further challenges in defining what this will look like in practice but we will continue to work with the industry to develop this. We will also continue to explore the governance options around an over the internet network with a view to make a decision on this in the near future.

13. We have decided that utilising ISO20022 as the basis for the pot matching and pot transfer message standards is the appropriate approach. We believe, from information presented to us in the technical group, that these standards can be defined within the timescales required and will facilitate a broader joined up approach to the messaging standards of automatic transfers.

14. It is our intention that the governance of these messaging standards should fall to the ISO20022 community. We believe the UKFMPG (UK Funds and Market Practice Group) is best placed to oversee these standards in a subgroup designed for this purpose. We would encourage pension industry representatives to engage with this group in the development of the messaging standards to ensure schemes and potential registers understand the data items required and any limitations of these standards.

Next steps

15. We are considering the regulatory framework we must develop, and what can be put in guidance alongside this for the technical model to function as intended. To that end we will be looking to set out the standards that any technical approach will need to meet.

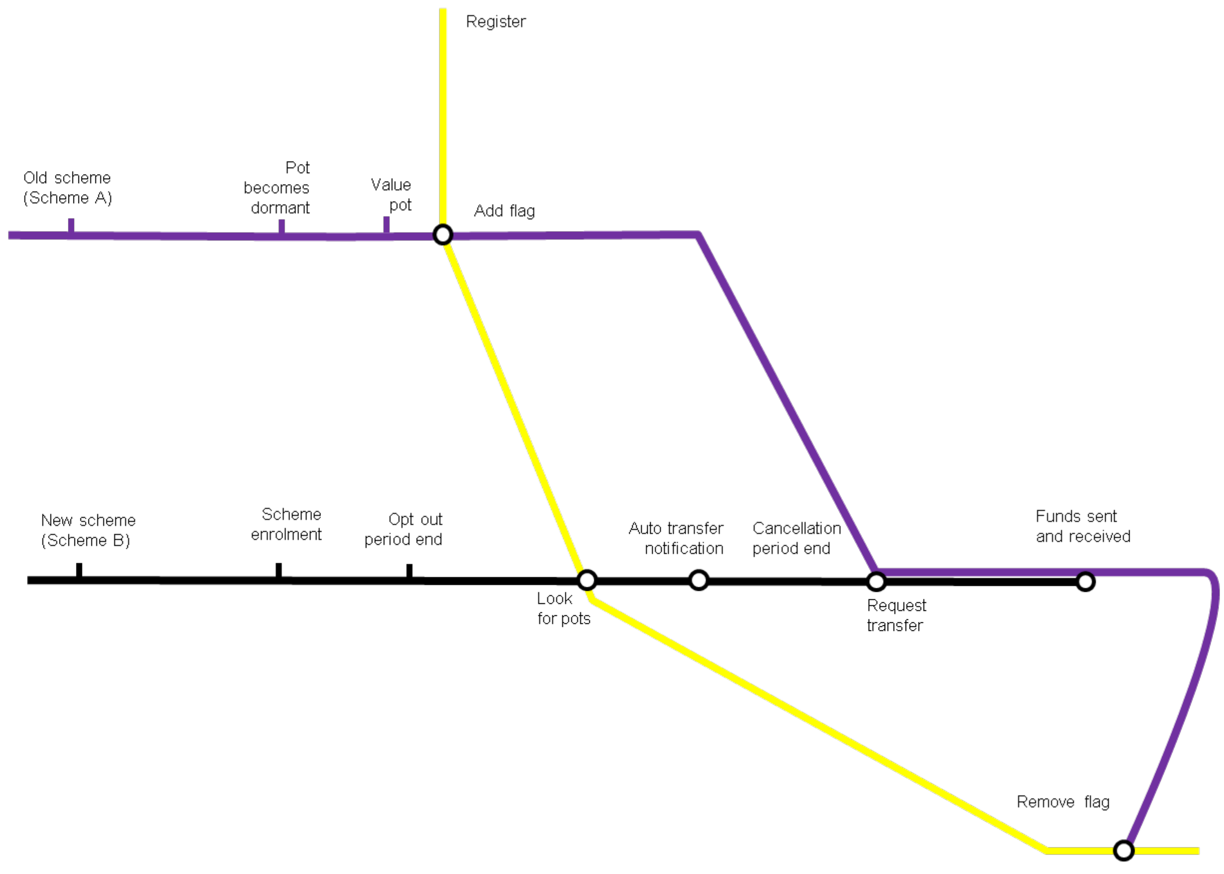
16. We continue to work through the details of these requirements with our technical and policy stakeholders and this will be our focus going forward. Particularly, this will include the following non-exhaustive list:
    a) Audit requirements of schemes and registers;
    b) Management information;
    c) Exception handling;
    d) Availability, security, and authentication;
    e) Details of the network operation and features.

Annex B: Step By Step Guide to Automatically Transferring Pensions

This Annex outlines the steps that different parties would take in the process of automatically transferring a small pot according to the implementation model that has been recommended to us.

This diagram provides a snapshot of the different interactions between these parties throughout a member’s journey from one employer and their pension scheme to another. The rest of this chapter explains the different actions taking place at each of the points of this journey.

AT actors and process



Pot Eligibility and Pots in Scope

Actors: **Schemes**
Registers

- To be included:
    - Pure money purchase benefits with an employer connection where the value is under £10,000 and where the pot has been deemed to be dormant and eligible according to the criteria below.
    - Pots where the first contributions were received on or after July 2012.
    - Pots accumulated in a charge-capped default arrangement.
- To be excluded:
    - 1 member schemes.
    - Executive Pension Plan.
    - Small Self-Administered Schemes (SSAS).
    - Pots that have been subject to a benefit crystallisation event.
    - Money purchase schemes with guarantees or promises (for example a third party promise).
- Additional Voluntary Contributions would not usually meet the definition of a qualifying scheme above – i.e. that it is in a default fund. As such we feel there is no need to explicitly exclude these.

Member Leaves Employment

Trigger point for Scheme A to assess whether pot is eligible to be automatically transferred.

Actors: **Employer A**
Scheme A

- For the purposes of the automatic transfer of pension pots, Scheme A should determine that a pot has become dormant if either of the following criteria are met:
  - Employer A informs the scheme that the member has ceased active membership; or
  - The scheme has not received contributions in the 12 months preceding an Annual Benefit Statement.
- This alternative check is aligned with the Annual Benefit Statement in order to avoid creating a new point at which schemes should check a member's contributions. Where an employer fails to inform the scheme the member has ceased being an active member and their final contribution is made just after an Annual Benefit Statement, their pot may not be deemed to have become dormant until up to 24 months after the member's final contribution.

Check Pot Eligibility

Scheme A checks whether pot is eligible to be automatically transferred.

Actors: **Scheme A**

- Scheme A will be responsible for checking the dormant pot against the eligibility criteria. For a pot to be eligible it must meet the eligibility criteria at section 1 above.
- Scheme A must carry out this assessment within 2 months of the pot becoming dormant.
- This is the only point at which the pot needs to be valued to determine whether it is eligible to be automatically transferred.

Add Flag

Old scheme flags details of eligible pot.

Actors: **Scheme A**
Register A

- Schemes identify pots that fulfil criteria for pot to be flagged.
- Schemes transmit (or make available) flagging data to their register.
- The flag must contain data items to allow for matching:
  a. At least two from; surname, initial, and gender.
  b. National Insurance Number.
  c. Date of birth.
  d. Pension Scheme Tax Reference (Scheme ID).
  e. Account ID (Pot ID).
  f. Employer name that member was enrolled onto the scheme with.
- Employer name will allow the member communication to include details of which employer the pension pot was saved through helping the member identify their pot.

Update Flag

Scheme updates flag.

Actors: **Schemes**
Registers

- Some events may require a flag to be updated, for example:
    - A scheme may be moved to a new provider.
    - New updated data could be received.
    - Update the data on the flag.

Remove Flag

Triggers for removing details of flagged pot.

Actors: **Scheme A**
Register A

- Flags will be removed from pots if any of the following happens:
    - Any new payments are received (excluding in-scheme refunds).
    - There is a benefit crystallisation event.
    - The pot transfers (this could be an automatic transfer or member initiated transfer).
    - The member dies.
    - The flag was recorded in error.
    - The size of the pot reduces to zero.

Member Starts New Job

Capture accurate data on employee.

Actors: **Employee**
Employer B

- Employer records employee data as they begin their new employment.
    - It is anticipated that this will be the most recent address information for the employee, ensuring that communications to the member are sent to the most recent address.

Pension Scheme Enrolment

Employer enrols employee into pension scheme and notifies employee they have been enrolled. Automatic enrolment opt-out period starts.

Actors: **Employee**
Employer B
Scheme B

- Employer enrols employee into pension scheme.
- Employer communicates with employee to let them know they have been automatically enrolled and how to opt-out.
- 1 month automatic enrolment opt-out period commences if the enrolment is automatic.
    - If employee opts out within this window no search will take place.
- Data captured by new scheme.

Pot Matching

Trigger point to search for pots

Actors: **Scheme B**
Register B

- The scheme gives their register the pot matching data and instructs the register to search for pots.
    - Commercial pressures may encourage schemes to search quickly as where there are competing requests, the first to transfer the pot will succeed.
    - We are considering the potential for further searches for matching pots on an on-going basis. This is a process we have referred to as pot sweeps.

Search for Matching Pots

Register B searches the register network for matching pots

Actors: **Register B**
All other Registers

- Registers will communicate in a way defined by a set of open standards that are under development.
- The searching register will search for pots on all other registers in the system.
- The searching register will also search on its own database.
- Responses will be sent to the searching register indicating there are either:
    - No matches; or
    - Details of matches made and associated data.

Pot Matching Results Delivered to Scheme

Register tells scheme results of search for matching pots

Actors: **Register B**
Scheme B

- Register will inform the scheme that matches have been made and data items to facilitate transfer.
- This will include the data that must be attached to a flag above.
    - Matching data of surname, initial, gender, National Insurance Number, date of birth.
    - Pension Scheme Tax Reference (Scheme ID).
    - Account ID (Pot ID).
    - Employer name.

Transfer Notification

New scheme notifies member that eligible previous pots have been matched

Actors: **Scheme B**
Register B

Under Phase 1 'Pot Matching / Opt-in Phase'

- Scheme receives notification of matches made for each pot (there may be multiple matched pots on any particular search).
- Scheme sends transfer confirmation form and notification of matched pots to the member with details on how to confirm a transfer.
- Member responds in accordance with the instructions on the communication.
- Scheme receives response from member that they consent to transfer taking place.
- Scheme initiates transfer, if appropriate.

Under Phase 2 'Full Rollout'

- Scheme receives notification of matches made for each pot.
- Scheme sends opt-out notification letter to member supplying appropriate information concerning the member's pension pot(s) and notifying them that unless they cancel within 30 days their pension pot(s) will be transferred to their new scheme.
- Scheme can start countdown of 30 days and then processes transfer if no confirmation of opt out is received.
- If notification of opt-out is received Scheme B must not transfer pot(s).

Transfer of Pension Pots

Member consents to transfer or doesn't opt out. This is the trigger point for Scheme B to request a transfer of pension pots.

Actors: **Scheme B**
Scheme A
Register A

- Schemes must use electronic payment methods.
- Receiving Scheme (Scheme B) contacts ceding Scheme (Scheme A) with transfer information. This will be details of pension pot and where to send the funds (i.e. BIC or account number).
    - Schemes may use their registers to perform this function if they wish.
- Scheme A then sends necessary reconciliation data and funds to Scheme B
    - This may be a consolidated payment to cover more than one pension pot with reconciliation information cross-referenced to this single payment.
    - To facilitate an automatic and cost efficient process this data must be provided in a standardised format.
- Scheme B contacts member to confirm transfer into fund.
- Scheme A instructs Register A to remove flag because pot has transferred.

Annex C: Membership of the Working Groups

All Groups are chaired by DWP

Co-ordination Group

Organisation
Friends Life
Legal and General
TISA
B&CE
Hargreaves Lansdown
The Pensions Regulator
Money Advice Service
The Pension Advisory Service
NEST
Aegon
Capita
NAPF
HMRC
JLT Group
ABI
FCA
Standard Life

Technical Team

Organisation
Aviva
Altus
TIISA Exchange (TeX)
Actuare
Calastone
Origo
NEST
The Pensions Regulator
SBC Systems
Legal and General
JLT Group
Accenture
SWIFT
Vocalink

SBC Systems and Legal and General don’t attend but hold a watching brief and receive all supporting papers

Policy and Legislation Team

Organisation
Altus
Legal and General
Towers Watson
The Pensions Regulator
Prudential
Calastone
7plc
SBCSystems
Standard Life
The Pensions Regulator
Origo
Payments Council
Zurich
Society of Pension Professionals
JLT Group
NEST
Mercer
Origo
FCA

Customer and Communications Team

Organisation
TPR
MAS
FCA
Scottish Life
Aviva
Friends Life
Warburtons
TPAS
Zurich
Whitbread