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16 November 2026

smallpots.policyteam@dwp.gov.uk

Issued by email

Dear all

Small Pots: a pathway for consolidation

I am writing on behalf of the Association of Consulting Actuaries in response to the above consultation.

We continue to support the Government's plans to address the small pots challenge, and to implement automated approaches to tackling this issue. Our detailed response is provided on the following pages and our key points are set out below:

- We consider the proposed 12-month threshold to be too short, as it could result in transfers being made in respect of members who take time away from work for parental leave, sabbaticals, or other career breaks. There is a risk that due to payroll cycles individuals could just fall into scope close to the cut-off point. Our preference would be 15- or 18-months.
- Harmonised regulatory requirements and targeted outcomes will be essential to deliver a coordinated member journey and ensure that standards are consistently high, regardless of whether a member is in a single employer trust, a master trust, or a contract-based scheme. There must be equal expectations for authorisation, consumer protection, service standards, supervision and exit.
- Member communications should be designed from day one to be clear and consistent (in use of language, presentation of information, and the overall journey).
- The framework must be economically viable. This requires an evidence-led, market-wide review of the flat-fee de minimis within a wider assessment of business models, competition, and pricing approaches (including cross-subsidies). This should be in the context of the General Levy and interaction with other key policies such as the scale test and Value for Money.

We hope that you find the contents of this letter of assistance. We would be happy to discuss them further if that is helpful. In this event, please contact me at tessa.page@mercer.com.

Yours sincerely

Tess Page
Chair of DC Committee
On behalf of the Association of Consulting Actuaries Limited

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APPENDIX

Consultation questions

Question 1: Do you agree with the proposals set out in this chapter? Are there any unintended risks or consequences that may arise from these proposals outlined above?

Scope

While we acknowledge the intention behind the pragmatic approach of having an initial focus on post-2012 pots in charge-capped default arrangements (which reduces exposure to some of the more complex features found in older arrangements such as with-profits funds), we believe that pots invested in self-select funds should also be brought into scope for small pot consolidation, supported by clear communications. The fact that a member has at some point selected their investments does not mean that they remain engaged with their pension investments, or are more likely to take an active decision now about consolidation. Additionally, some members have investments in both default arrangements and self select funds, within the same scheme.

Time threshold

Regarding the proposal of a 12-month threshold, we believe this is too short and could result in transfers being made in respect of members who take time away from work for parental leave, sabbaticals, or other career breaks. While one-year absence periods are perhaps more "normal", there is a risk that due to payroll cycles individuals could just fall into scope close to the cut-off point. Our preference would be 15 or 18 months.

Question 2: Can schemes reliably identify pots that have guarantees attached? Are there operational or administrative risks that could threaten the effective retention of guarantees for members. For example, data quality?

Most schemes are able to identify pots that have guarantees attached, though this does vary by scheme and relies on good data quality and governance standards and there is no common approach to flagging such guarantees on administration records. There is also the potential for schemes to believe there "may be" guarantees attached to pots, notably for legacy with-profits arrangements, only to find on further review that they don't, or that the guarantees are relatively lacking in real value. This risks excluding pots from the scope of consolidation for reasons of over-caution or poor data. We would also argue that below a certain asset value, guarantees may be negligible in monetary terms.

To give schemes confidence in the treatment of benefits with guarantees, we believe it would be helpful for the Government to introduce industry-wide classification standards which providers of products with guarantees would be subject to – this would allow a cleaner flow of data from providers (often legacy in nature) to scheme administrators and governance bodies to accurately identify guaranteed benefits.

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Question 3: Are there any guarantees or protections that should automatically be out of scope from trustee and scheme manager discretion?

If the Government moves ahead with an initial focus on post-2012 DC default arrangements, this should limit the potential exposure to complex guarantees and protections, but their existence will still need to be evidenced. We recommend that protected pension ages, enhanced tax-free cash, guaranteed survivor benefits, and guaranteed underpins should be considered as out of scope of consolidation and "regular" discretion though it would be sensible to permit trustee discretion as backstop option for exceptional cases, allowing trustees the flexibility to act where they have a genuine basis for doing so, rather than requiring bespoke assessments of every small pot.

Question 4: How frequently does the situation arise where preservation of a PPA must be considered? Do you think the proposed approach would work administratively, or is there a better way of achieving the same outcomes for members?

We do not have statistics on the prevalence of PPAs but believe greater market understanding would be valuable and encourage the Government to progress data gathering, distinguishing the post-2012 cohort from the wider market.

Where a PPA exists and cannot be preserved on transfer, the pot should be excluded from scope (per our comments to Q3). A standard protection indicator and proportionate evidence requirements would help this process to operate smoothly and avoid excessively onerous analysis and repeated legal opinion of individual small pots.

Question 5: Are there any additional guarantees or protections that will need to be considered that have not been outlined in this consultation?

Within this category we believe the following should be considered:

- Linked DB and DC benefits within hybrid schemes (where DC pots are often used for PLCS purposes)
- Enhanced tax-free cash
- Scheme-specific retirement terms
- Exit penalties / market value adjustments
- Subsidised / zero member borne charges.

Standardisation of data fields would support identifying these arrangements for both ceding and receiving schemes.

Question 6: Do you agree that the proposed content of the pre-consolidation notice would provide members with sufficient information to understand the consolidation process and support informed decision-making, while remaining clear, proportionate and accessible? How do you consider what would be best to test and review this communication?

We support the proposed content but consider this just one part of a broader member journey. Standardising the terminology (for example, a pension pot may be referred to differently by different schemes – pot, fund, account, value, etc), the order of the information presented, and the action steps will go a long way to helping members who may well receive multiple communications of this nature.

We favour a one-page summary that covers the critical information, with further details layered behind this rather than turning the notice into a lengthy pack.

The potential for scams is a key concern. Scam awareness and sensitivity should be a core design requirement, and genuine communications should offer a way for individuals to validate the notice easily without needed a link or QR code (which can raise suspicions).

We further recommend consumer testing of comprehension, ease of action, accessibility, and scam resilience. The testing approach being used ahead of the launch of pensions dashboards is a good example of the industry and savers providing useful input in a pilot phase.

Question 7: In your view, is there any additional information that should be included in the notice, or any information proposed that is unnecessary, overly complex, or could be presented differently? Please provide reasons and evidence where possible.

We have no suggestions for further information and again recommend a one-page summary as the core of the notice.

Standards should be established to prevent any "marketing" of the consolidator, and the notice should not imply a personal recommendation, or use design features to make one option artificially prominent.

Question 8: In your view, where a member already has an allocated consolidator scheme, should they be able to choose an alternative consolidator for subsequent consolidations (option 1), or should subsequent eligible deferred pots transfer by default to their existing consolidator scheme (option 2), subject to the member's right to opt out and the scheme remaining an authorised consolidator?

We prefer option 2. This is most consistent with reducing fragmentation and helps to avoid re-creating a member's previously scattered pots on a fragmented basis again. Giving members repeated options also puts more weight on active decision-making within a policy that aims to look after disengaged savers through a strong default.

The communication should nevertheless preserve meaningful choice. If the member actively selects a different consolidator, Government should explore whether previously consolidated pots should also move to the newly chosen scheme. This could allow the member to change their preferred destination without recreating the fragmentation that the policy is intended to address

Question 9: Do you have any other views on the proposed member communications journey, including the design, timing, format, delivery, accessibility or operation of communications under the Multiple Default Consolidator solution?

No further comments.

Question 10: Do you agree with the proposals set out in this chapter? Are there any unintended risks or consequences that may arise from these proposals outlined above?

We support the starting point that consolidators should meet high and consistent standards. Authorised consolidators will receive money through an automated process, and will be the home for pension pots that belong to unengaged savers. This justifies requirements for first class governance, financial sustainability, operational capacity, and the ability to deliver good value for members.

We would be cautious of bringing consolidators (in that role) into the immediate scope of the new Value for Money framework and provider scale requirements at this early stage (though this could be a longer-term consideration) – these arrangements are fundamentally different to ongoing workplace pension providers and schemes and their metrics for aspects such as service will not be comparable. The VFM framework remains untested and burdening consolidator vehicles with a new piece of legislation that will be a significant exercise would be a distraction at this stage.

Regulatory alignment on standards is also important. We believe that the DWP, TPR and the FCA should publish a joint cross-market approach so that legal differences do not produce incompatible operating rules or materially weaker protection. The authorisation framework should also recognise that consolidators may both receive and cede pots and should require readiness for that two-way activity.

Question 11: Do you consider that there should be other terms of the scheme that are explicit requirements in order to act as a consolidator scheme?

Schemes should have credible arrangements for the orderly transfer of members if they cease to qualify as a consolidator. "End game" scenarios and requirements should be clearly established before they arise.

Question 12: Do you consider the existing requirements relating to financial sustainability to be sufficient as an assessment of the scheme's ability to absorb the operational and financial implications of acting as a consolidator?

The existing financial sustainability requirements offer a good baseline, but financial sustainability should be considered alongside the specific operational and financial implications of acting as a consolidator. Financial resilience is not the same as operational capability and these things should be assessed together without creating a duplicative regulatory regime.

The current Master Trust authorisation framework provides a foundation for trust-based schemes, while contract-based providers are subject to FCA requirements regarding financial resources. We therefore do not believe a full new and separate regime is necessary. Instead, the existing financial sustainability frameworks could be supplemented with consolidator-specific tests around the ability to process the expected inflows, operational capacity, and servicing requirements for what will be a relatively unique population.

Question 13: Which approach to scale do you consider most appropriate to support positive member outcomes, and why? Are there alternative approaches that should be considered? How should this be monitored and updated over time to ensure they remain appropriate as the market develops?

Scale is not synonymous with quality, and we continue to believe that good member outcomes should be the goal, rather than arbitrary scale targets.

A scheme at scale or on the scale transition pathway should not automatically qualify as a consolidator – it must be able to meet the operational and consumer-protection standards from the point at which it begins receiving small pots, which may be a very different operation to its current customer base. On the other hand, a provider delivering strong outcomes with the operational capability to handle small pots should not be excluded just because it scale is currently below peers – albeit we expect long-term scale. We would welcome new entrants to this market in the UK (potentially with global experience) who may take some time to reach scale.

We believe the assessment should therefore combine a minimum scale guideline with operational readiness, financial sustainability, governance, and service standards.

Government should also periodically review market competition as consolidators develop. Any concerns that credible entrants are facing barriers to entry should be investigated quickly and appropriate amendments to the framework considered.

Question 14: Do you agree that the most appropriate and equitable approach is to review the flat fee de minimis threshold across the market as a whole, with any changes implemented ahead of the introduction of the Multiple Default Consolidator solution? If not, which of the options discussed do you consider most effective in delivering strong member outcomes, and why?

Flat fees exist in part to cover the minimum cost associated with administering and servicing a pension pot, regardless of its size. A percentage charge on a small pot may not recover that cost. The intended review should therefore consider the costs of administering small pots, the extent of cross-subsidy between members, and the interaction with the General Levy and other per-member regulatory costs.

We urge this review to be completed before consolidator authorisation and commercial decisions are finalised. If the evidence supports a longer-term move away from combination charging, this should be considered alongside reform of the General Levy and phased over time once the small pots solution is in place and the effects of dashboards, scale and VFM reforms are clearer. The market in 5-years time is likely to look very different to how it looks now. While the in-flight reforms play out, the full effects of pricing changes may not be apparent. Therefore, early modelling should inform the policy direction but with a staged transition only when experience of the reformed market supports it, with sufficient notice to inform and protect members and scheme sustainability.

Question 15: Do you think schemes should be prohibited from acting as a consolidator scheme if they do not receive a specific VFM rating, if so, what rating do you consider to be an appropriate level of value?

The consolidator regime should be aligned closely with the final VFM framework but we would caution having automatic consequences while the new VFM process is untested and immature.

Once there is confidence that the new VFM framework is working effectively and can be applied to consolidators, the Dark and Light Green ratings would seem a suitable requirement

Where a consolidator falls below the expected standard, our preference would be to restrict receipt of new pots while review and remediation is undertaken, rather than automatically requiring existing consolidated pots to be moved which could be unnecessarily disruptive if a clear and quick improvement plan can be implemented.

Question 16: Do you agree that consolidator schemes should undertake same scheme consolidation, and that option 1 presents the best safeguards for savers? Do you agree with the proposals on exclusions from same scheme consolidation?

Yes, and we believe option 1 to be a sensible starting point. Consolidators should demonstrate that they can bring together eligible internal pots without removing guarantees, protections, material investment choices (where mapping is not obvious and could incur material costs) or linked benefits.

Authorisation should require an evidenced capability and a credible implementation plan, rather than completion of every legacy case regardless of legitimate exclusions or technical complexity..

Question 17: Do any of the options explored in this chapter present potential challenges specifically for contract-based schemes if the FCA were to introduce identical requirements in its rules?

The perhaps obvious difference is that contract-based schemes involve contracts with individual members. Requirements for consolidation without explicit consent should therefore provide appropriate legal certainty.

Our experience is that contract-based providers feel more hamstrung by disclosure requirements, which are not always member-focused. This will be a challenge from a member comprehension perspective if communications from ceding contract schemes look and feel very different to those from trust schemes. We therefore support equivalent standards and outcomes and encourage the regulators to publish a joint comparison showing how cross-market parity and interoperability will be achieved.

Question 18: To what extent do you agree that existing regulatory powers and supervisory frameworks, together with the proposed supervisory and intervention powers, provide a sufficient basis for the effective ongoing oversight of consolidator schemes? Please provide reasons for your answer, including whether there are any additional supervisory or intervention powers that should be considered, or any proposed interventions that you do not support

The existing powers and supervisory frameworks provide an excellent foundation, in our view, one that has been enhanced and strengthened significantly over the last decade. These frameworks should provide the basis of oversight of consolidators, rather than drafting new frameworks and standards. Regulators should have the flexibility to require additional reporting that is relevant to consolidators, operational improvements / disclosures, and restrictions on new allocations and management of transfers in flight.

Question 19: To what extent do you agree with the proposed approach to the treatment of members' pots following the loss of consolidator status? Please provide reasons for your answer, including whether you consider a single approach, or an alternative approach, would better support member outcomes.

- A one-size-fits all will not be appropriate. Where the issue is temporary or remediable, we do not believe transfers away should be automatic.
- We would favour ceasing new allocations and placing existing pots under enhanced supervision. Where the issue is terminal, including where a provider chooses to voluntarily exit the market, an orderly transfer will be appropriate.
- A voluntary exit should be considered in the context of the carousel and capacity of the remaining market. The regulator and oversight body should be able to coordinate the removal of the exiting consolidator from allocation processes and manage the impact on other schemes, rather than allowing operational consequences to emerge only after notice is given.

Question 20: To what extent do you agree that decisions on the removal of consolidator status should remain subject to regulatory judgement on a case-by-case basis? Are there any breaches that you consider should automatically result in the removal of consolidator status?

We are comfortable with the approach set out. Regulatory judgement is appropriate because sudden, automated removal could destabilise a concentrated (and initially immature) market.

Automatic removal should be confined to significant events such as loss of authorisation, fraud, or insolvency. A remediable operational or service issue should not automatically result in removal.

Question 21: To what extent do you agree with the proposed approach for schemes wishing to voluntarily exit the consolidator market? Please provide reasons for your answer, including whether you consider an alternative approach, would better support member outcomes.

We believe the proposed approach is sensible, provided exit requires regulatory approval, adequate notice, and a funded operational plan covering existing pots, transfers in progress, communications, data reconciliation and costs. Communications should distinguish an orderly voluntary exit from regulatory failure.

Question 22: How do you consider this process should be delivered for smaller schemes that are unlikely to transfer significant volumes of small pots and for which investment in dedicated digital infrastructure may not represent good value for their wider membership?

Smaller schemes should still be able to meet the requirements through their existing provider or administrator (who will likely be implementing the process across their wider book), rather than being expected to invest in new infrastructure themselves. We don't think this requires a separate framework or approach for smaller schemes.

However, consideration should be given to in-house administrators for single employer trusts, who have specific needs and will not have immediate access to the scale and learnings from a wider base of schemes. Engagement with those schemes will help to prepare for launch.

Question 23: To what extent do you agree with the government's proposed approach of a federated model supported by a central oversight body? What factors should the government consider when determining where the central oversight function should sit, including whether it should be delivered by a public body, an existing organisation, or an industry-led body operating within a statutory framework?

The federated model offers a sensible approach to delivery by 2030, provided its key functions are defined proportionately. Existing transfer and service capabilities should be leveraged where they meet common standards; new central infrastructure should address an evidenced gap rather than duplicate existing capabilities.

The central oversight body should be independent, regulated, transparent, and accountable. We have a slight preference for a public body that potentially leverages resources from the existing regulators, supported by industry engagement (for example, through the use of working groups). The body should not be funded or controlled in a way that gives a small group of consolidators undue influence over standards or access.

The principal gap in our view is programme-level responsibility for the complete transfer journey, including the role of ceding schemes (including their various stakeholders such as trustees, governance committees, and employers), consolidators, and administrators. Before firms commit to system builds, DWP should identify who will coordinate stock migration, major-provider sequencing, common transfer conventions, reconciliation and transfers in flight. If the oversight body directs timing or reallocates pots, its legal authority, accountability and liability must be explicit. If its remit ends at discovery and allocation, another named party must own the remaining coordination.

Question 24: Do you agree that detailed technical and operational standards should be capable of being updated outside legislation, subject to appropriate governance and consultation?

Yes, subject to appropriate industry consultation (both initially and ongoing).

Question 25: To what extent do you agree that legislation should require pension schemes to comply with common data standards when participating in the Multiple Default Consolidator solution? In particular we are keen to understand:

- **what matters should be included in legislation, and what matters should be left to technical standards or statutory guidance?**
- **what data items are likely to be essential to support accurate matching and transfer activity under the Multiple Default Consolidator solution?**

Consistent standards will be essential to support accurate matching and to reduce the risk of inappropriate transfers / missing transfers that should take place. The legislative framework should establish an obligation to comply with prescribed standards, together with appropriate requirements for data quality, security, auditability and governance. This will have wider benefits for the pensions industry more generally.

Our preference would be not to include the very specific requirements (data fields, formats, technical specifications, etc) in primary legislation. These should instead be set out through statutory guidance, allowing the framework to evolve and flex as experience and technology develops.

Question 26: To what extent do you agree that pension schemes should be required to use approved messaging standards when participating in the small pots framework? In particular we are keen to understand:

- **what role should legislation play in establishing messaging requirements, and what matters should be left to standards or governance arrangements?**
- **how should the framework ensure that approved messaging arrangements are accessible to schemes and providers across the whole market?**

We agree that the use of approved messaging standards would be beneficial. The legislation should set out the framework, but not the detail as that will change over time and needs to be flexible enough to adapt to future changes and innovations.

Question 27: To what extent do you agree that pension schemes should be required to apply a common data matching framework when participating in the small pots consolidation process? In particular we are keen to understand:

- **are there specific aspects of data matching that should be prescribed in legislation, or should detailed matching criteria be set through standards overseen by the central oversight body?**
- **what safeguards should apply where a possible match is identified but cannot be confirmed automatically?**
- **what information should schemes be required to exchange in order to identify the correct destination consolidator while minimising unnecessary data sharing?**

A common matching framework will be necessary to provide consistency and reduce the risk of inappropriate transfers.

A possible match that cannot be confirmed should pause. Parties should exchange only the additional information needed, with review and member contact where necessary. The framework should not shift routine matching responsibility onto disengaged members. Matching standards should align with dashboards and wider transfer work wherever possible to avoid duplication.

Question 28: To what extent do you agree that a carousel allocation process should be used where a member does not already have a pot with a consolidator? In particular we are keen to understand:

- **what factors should be taken into account when designing the carousel to ensure that it is fair, transparent and effective?**
- **what information should be used to determine which consolidator holds the member's largest pot, and how should that information be verified?**

A carousel is needed where there is no existing consolidator relationship, but must be thoroughly tested. A distributed carousel applying identical rules may achieve a sufficiently even outcome at lower cost, whereas central operation creates another message and points of dependency.

Whichever model is chosen, the rules must be transparent and capable of audit, with ongoing monitoring of allocation and concentration. Participants will need a mechanism to involve new consolidators and remove closed / exiting providers.

The detailed allocation methodology should be capable of being amended through appropriate governance arrangements without requiring legislative change.

Question 29: To what extent do you agree that a central digital interface should maintain a list of consolidator schemes, including verified contact details and relevant information?

We agree that the central digital interface should maintain an authoritative register of participating consolidators. This should include adequate information to enable schemes to identify authorised consolidators and communicate with them securely and efficiently.

It will be essential to ensure that the information is accurate and up-to-date. To deliver this, clear responsibilities should apply for maintaining the interface, with consolidators required to notify the central body promptly of material changes and/or confirm no changes.

The register should also provide appropriate audit and version-control functionality, enabling schemes to demonstrate which information they relied upon when initiating a transaction.

Question 30: To what extent do you agree that a central digital interface should issue, or enable the issuing of, security credentials, certificates, keys or tokens to support secure communications between participating schemes and consolidators?

We do not have comments on this question.

Question 31: To what extent do you agree that the proposed requirements provides a proportionate basis for pot matching and contact? Please provide reasons for your answer. Are there any additional data fields that should be included in the requirements to support more effective pot matching, and if so, why?

The proposed requirements appear proportionate, and many employers will be regularly asking for updated information for other purposes anyway. The key here is to ensure the additional requirements are not administratively cumbersome and are easily collected and submitted. The 12-month window to comply with the duty is a suitable timeframe.

In relation to the updating of records every 12 months, it may be appropriate to have a 'window', so that the employer can use data that they might have gathered as part of another information gathering exercise. This approach will reduce both the cost and burden on employers.

Question 32: To what extent do you agree with the proposed approach to improving member data quality through enhanced employer data requirements? Please provide reasons for your answer, including whether the proposed 12-month interval and information requirements are proportionate, whether any additional information should be included or any proposed information is unnecessary, and how any administrative burden on employers could be minimised.

While we welcome initiatives to improve data quality, we are not convinced that the proposed employer duties are proportionate or necessary. For instance, we see little value in requiring employers to re-capture date of birth. This is already a required data item on enrolment and, unlike name or contact details, will not change.

In some instances, the proposals may be impossible – for example a current employer cannot resolve stale records held by a scheme from an earlier employment, even though those deferred pots are central to this policy. Government should assess separate routes for improving historical records, including lawful use of government data and opportunities arising from pension dashboards, without assuming dashboards will automatically correct scheme records.

Any new employer duty must be aligned with the scheme's dormancy decision and delivered early enough to prevent an incorrect notice. Government should explain how information will flow through payroll and administrators, how corrections are made and what happens when employer and scheme records conflict. Without that operational design, it is difficult to judge whether the proposal is proportionate.

Question 33: To what extent do you agree with the proposed approach requiring employers to provide information where an individual is temporarily absent from work but intends to return and resume pension contributions? Please provide reasons for your answer, including whether you agree that such information should be used to help schemes avoid incorrectly treating pots as dormant.

We do not believe that detailed statutory reporting by employers is the most proportionate or effective mechanism. Employers may not know a member's future intentions or return date, and manual intervention could be costly and prone to operational risks.

A simple employment-status indicator through existing data flows may be more workable than reporting future intentions or precise return dates. Our recommended longer dormancy period (15- or 18-months) should be tested against this alternative, including the extra servicing and potential

levy costs of retaining pots longer. Employers should be responsible only for information reasonably held, not for subsequent changes to a member's plans.

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