

EXPLANATORY MEMORANDUM TO
THE OCCUPATIONAL PENSION SCHEMES (CHARGES AND GOVERNANCE)
(AMENDMENT) REGULATIONS 2022

2022 No. 10

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument introduces a new restriction on the permitted charges that trustees or managers of certain occupational pension schemes can impose upon their members, for the investment administration and general scheme administration of their pension savings (also known as “rights”) in the default fund.

2.2 This new restriction applies to the flat-fee charges which can be levied on members of a defined contribution pension scheme used for automatic enrolment with rights invested in the pension scheme’s default fund. It prohibits a flat-fee charge from being imposed on a member which would reduce the value of the member’s rights in the default arrangement¹ to less than a £100 threshold – or de minimis. There are three different definitions of default arrangement under regulation 3 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015² (S.I. 2015/879) (“the Charges and Governance Regulations”) but broadly speaking, a default arrangement means an arrangement into which members’ contributions are invested and the member hasn’t expressed a choice as to where their funds should be invested.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is Great Britain.

4.2 The territorial application of this instrument is Great Britain.

4.3 The Department for Communities in Northern Ireland will be producing its own legislation replicating this instrument for Northern Ireland.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

¹ <https://www.legislation.gov.uk/ukdsi/2015/9780111128329/regulation/3>

² <https://www.legislation.gov.uk/ukdsi/2015/879/introduction>

6. Legislative Context

- 6.1 Schedule 18³ to the Pensions Act 2014 (c. 19) allows the Secretary of State to make regulations which set limits on, or prohibit types of administration charges, including the flat-fee component of the combination charge.
- 6.2 The Charges and Governance Regulations make provision about what charges may be imposed in relation to qualifying schemes⁴, which is defined in section 16 of the Pensions Act 2008 (c. 30) as an occupational pension scheme, or a personal pension scheme, which is registered under Chapter 2 of Part 4 of the Finance Act 2004 (c. 12).
- 6.3 The Charges and Governance Regulations apply to those defined contribution occupational pension schemes offering money purchase benefits used by employers to meet their duties under automatic enrolment (“qualifying pension schemes”). Money purchase benefits⁵ are defined in sections 181 and 181B of the Pension Schemes Act 1993 (c. 48). Broadly speaking they are benefits where the member’s pension is solely based on their contribution and investment return, less costs and charges.
- 6.4 The Charges and Governance Regulations also apply to stakeholder pension schemes when they are used as qualifying pension schemes.
- 6.5 The trustees and managers of a qualifying pension scheme will be able to impose a flat fee charge on a member with rights in a default arrangement where the member has agreed under regulation 9 of the Charges and Governance Regulations⁶ that they can be charged in excess of the charges permitted for services or advice.

7. Policy background

- 7.1 Defined Contribution occupational pension schemes use charges to cover the costs of investing and administering members’ pensions. Under the Charges and Governance Regulations there are three permitted charging structures:
- a single percentage charge of the pot value, taken at the end of each year and capped at 0.75% of funds under management.
 - a combination of a percentage charged on each new contribution made, plus an annual percentage of funds under management charge; and
 - a combination of a monthly or annual flat fee plus an annual percentage of funds under management charge.
- 7.2 At present, where a flat-fee charge is levied, that charge applies irrespective of whether the member is active (continues to make contributions into their pension pot) or deferred (not making contributions to their pension pot). This means that some members, particularly deferred members could have their pension savings depleted to zero before they reach retirement.
- 7.3 To minimise the effect of erosion of members’ rights the Government is, by virtue of new regulation 6(5) of the Charges and Governance Regulations, introducing a £100 de minimis on the flat fee component of the combination charging structure, below which flat fee charges cannot be imposed.
- 7.4 This means that from 6 April 2022, if a members’ rights within their qualifying pension scheme’s default arrangement is £100 or less, they will be protected from

³ <https://www.legislation.gov.uk/ukpga/2014/19/schedule/18>

⁴ <https://www.legislation.gov.uk/ukpga/2008/30/section/16>

⁵ <https://www.legislation.gov.uk/ukpga/1993/48/contents>

⁶ <https://www.legislation.gov.uk/ukdsi/2015/9780111128329/regulation/9>

incurring a flat fee charge. If those rights are above the de minimis threshold of £100, then new regulation 6(6) will provide that a flat fee charge can be imposed, provided that the imposition of that charge does not result in reducing the value of the members' rights to less than £100.

- 7.5 New regulation 6ZA(1) and (2) clarifies that where more than one flat fee charge is imposed on a member's rights under the default arrangement within a single charges year, the member's rights must be restored to its true value as soon as practicable.
- 7.6 New regulation 6(7) provides for the value of a member's rights for the purposes of the de minimis provisions in regulation 6(5) and (6) to include the value of any refund or rebate to which the member is entitled in accordance with regulation 6ZA to restore the member's rights to its correct value.
- 7.7 Additionally, new regulation 6ZA(3) requires trustees and managers to consider, where they are restoring a member's rights, the restrictions under regulation 5(3)(b) to calculate flat fee charges with reference to a period of time, whilst also keeping within the £25 limit specified in regulation 6(4)(a).
- 7.8 The above measures will ensure that members in scope gain some protection from erosion of their pension savings where flat fee charges are imposed by their qualifying pension scheme provider.

8. European Union Withdrawal and Future Relationship

- 8.1 This instrument does not relate to withdrawal from the European Union or trigger the statement requirements under the European Union (Withdrawal) Act

9. Consolidation

- 9.1 Informal consolidated text of instruments is available to the public free of charge via 'the National Archive' website <https://www.legislation.gov.uk/>.

10. Consultation outcome

- 10.1 The Review of the Default Fund Charge Cap and Standardised Cost Disclosure (Charges Review)⁷ included a call for evidence, which sought views on the need to protect scheme members with small pension pots, particularly small deferred pots, which are subject to a flat fee charge, from the risk of having their pots eroded, possibly to zero. That call for evidence found broad support to protect these small pension pots.
- 10.2 In the Government's response to the Charges Review⁸, published on 13 January 2021, the Department made a commitment to introduce a £100 de minimis on flat fees and to seek stakeholder views on this proposal.
- 10.3 On 24 May 2021, the Department published the results of its consultation "Permitted Charges in Defined Contribution Pension Schemes"⁹. In this document, the

⁷ <https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure>

⁸ <https://www.gov.uk/government/consultations/review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure/outcome/government-response-review-of-the-default-fund-charge-cap-and-standardised-cost-disclosure>

⁹ <https://www.gov.uk/government/consultations/permitted-charges-within-defined-contribution-pension-schemes>

Department set out proposals to protect small pots in default arrangements from erosion to zero. This consultation also presented the draft Regulations to implement this change. The following proposals were outlined in the consultation document:

- The de minimis will apply only to the flat fee charge element of the combination charge.
- The other element of this combination charge – a percentage charge based on the member’s value of funds under management, is unaffected by the de minimis, and may continue to be charged on any value pot.
- The de minimis will initially be set at £100. A pot of this value or below will not attract a flat fee charge.
- Where a member has multiple pots within the same provider’s default arrangement, the assessment of whether a flat fee should be charged upon that member’s rights, will be based on the combined value of those pots (the member’s rights), rather than on the separate value of the individual pots. In such a scenario, a flat fee can only be levied once per member in a single charges year.
- Where a member has several small pots of £100 or less with different pensions providers, for which a flat fee is chargeable, then the de minimis will be applied according to the value of the member’s pension pots (their rights) in the default arrangements for each provider.

10.4 We received 32 written responses from pension industry representatives, consumer representatives, trade unions, legal firms, actuaries, and one member of the public. During the consultation period, the Department held a number of stakeholder meetings to discuss the draft Regulations.

10.5 There was overall support from respondents for the de minimis to apply to both active and deferred pension pots. However, responses varied in terms of the level at which the de minimis should be set. £100 strikes a balance between protecting members, especially those with small pots, and maintaining the financial sustainability of scheme providers.

10.6 The majority of respondents agreed that the draft Regulations do achieve the policy intent. However, to address minor discrepancies identified by respondents between the policy proposed in the consultation document and draft Regulations the following amendments to the Charges and Governance Regulations were identified through the consultation:

- Clarification that a proportion of a flat fee may be levied on the value of a member’s rights, provided that the application of the partial fees will not reduce the value of the member’s rights to below £100.
- Clarification that where a flat fee is deducted more than once per member, per valuation period, within the same default fund, the provider must take steps as soon as is practicable to restore the members’ rights to the position it would have been had a single charge been deducted).
- Emphasis that the value of the members’ rights under the default fund for the purposes of the application of the new restrictions on flat fees, includes any rebates or refunds applied by the provider

10.7 The Government's response to this consultation can be found on the Gov.uk website¹⁰.

11. Guidance

11.1 The Charge Cap: guidance for trustees and managers of occupational schemes¹¹ has been updated to reflect the de minimis measure. The revised version will be published when the amending Regulations are being laid.

11.2 The Pensions Regulator (TPR) will be updating the guidance on its website to help trustees and managers of qualifying pension schemes understand their duties under regulation 6ZA of the Charges and Governance Regulations.

12. Impact

12.1 The impact on business, charities or voluntary bodies is principally on the pensions industry, specifically qualifying Defined Contribution Occupational Pension Schemes used for automatic enrolment that levy flat fees on their members.

12.2 The Equivalised Annual Net Direct Cost to Business for this measure is £6.6m.

12.3 Costs principally stem from requiring qualifying pension schemes in scope to familiarise with the new regulations, update and test their systems to stop charging pots worth less than £100, communication and market costs associated with the change and the ongoing loss of revenue from no longer being able to impose charges on pots worth less than £100.

12.4 There is no, or no significant, impact on the public sector.

12.5 A full Impact Assessment is submitted with this memorandum and published alongside the Explanatory Memorandum on the legislation.gov.uk website.

13. Regulating small business

13.1 These Regulations will impact any provider that offers workplace pension schemes used for automatic enrolment and levies flat fee charges. This may include small and micro pension businesses although most small businesses do not administer their own pension schemes, but instead use an external provider to meet their duties. TPR found that of the 28,360 schemes in the Defined Contribution market, 22,350 (79%) have identified themselves as relevant small scheme (RSS) or an executive pension plan (EPP) with 12 members or less.

13.2 The Department acknowledges that employees automatically enrolled into a pension schemes may have little or no choice over the scheme they are in, and by including small and micro businesses ensures all members have a degree of protection for their pension savings.

13.3 Of the six schemes identified in the Pension Charges Survey 2020¹² none are small or micro businesses. As reported in the Pension Charges Survey 2020 flat fees have become more common in recent years and particularly for larger Master Trusts

¹⁰ <https://www.gov.uk/government/consultations/permitted-charges-within-defined-contribution-pension-schemes>

¹¹ <https://www.gov.uk/government/publications/the-charge-cap-guidance-for-trustees-and-managers-of-occupational-schemes>

¹² <https://www.gov.uk/government/publications/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes>

pension providers, therefore it is unlikely that they are used by small or micro businesses.

14. Monitoring & review

- 14.1 The instrument does not include a statutory review clause. This is because we do not believe it is appropriate to commit to a formal statutory review of the de minimis measure in view of the interaction of this policy with any prospective solutions to tackle the proliferation of small pots and any potential future reform of the permitted charging structures.
- 14.2 In line with the requirements of section 28(2)(b) of the Small Business, Enterprise and Employment Act 2015 (c. 26), Guy Opperman MP, Parliamentary Under-Secretary of State for the Department for Work and Pensions, has made the following statement:
“Having had regard to the Statutory Review Guidance for Departments¹³ published under section 31(3) of the Small Business, Enterprise and Employment Act 2015, in my view, it is not appropriate to make provision for reviewing in the Occupational Pension Schemes (Charges and Governance) (Amendment) Regulations 2022”.
- 14.3 However, we recognise the importance of monitoring and evaluating the initial impact of our Regulations. We intend to review the impact of the de minimis informally through engagement with the Pension industry and non-industry stakeholders.

15. Contact

- 15.1 Fatou John, Department for Work and Pensions, email Fatou.John@dwp.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Joanne Gibson, Deputy Director for Automatic Enrolment and Defined Contribution Pensions Policy, at the Department for Work and Pensions can confirm this Explanatory Memorandum meets the required standard.
- 15.3 Minister for Pensions and Financial Inclusion (Parliamentary Under-Secretary of State), Guy Opperman MP at the Department for Work and Pensions can confirm that this Explanatory Memorandum meets the required standard.

¹³ <https://www.gov.uk/government/publications/small-business-enterprise-and-employment-act-statutory-review-requirements>