



DC funds and the Pension Schemes Bill: scale and asset allocation requirements

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Pension Schemes Bill requirements



Main scale default arrangements of multi-employer workplace DC pension schemes



£25 billion assets in the main scale default arrangement



By 2030 (subject to reliefs)



Government power to legislate to mandate that schemes must invest a proportion of assets “qualifying assets”

MSDA approval

Regulator may approve in respect of the main scale default arrangement (**MSDA**) if the master trust/GPP meets

- the scale requirement in respect of the MSDA, and
- any other prescribed conditions

What is the MSDA?

an arrangement -

- a) that is used for the purposes of one or more pension schemes, and
- b) subject to which assets of any one of those schemes must under the rules of the scheme be held, or may under those rules be held, if the member of the scheme to whom the assets relate does not make a choice as to the arrangement subject to which the assets are to be held.

The scale requirement

Value of
assets
at least
£25bn

Cannot come
into force
before 2030

Other
prescribed
conditions

Exceptions and relief

- Arrangements designed to meet the needs of individuals with protected characteristics
- Transition pathway relief
- New entrant pathway relief

Asset allocation

Regulator may approve in respect of the asset allocation requirement if it considers that at least the **prescribed percentage** (by value) of the assets held in default funds of the scheme are **qualifying assets**.

“it is somewhat unusual for a power to be in legislation with an express intention from the minister not to use it.”

Association of Pension Lawyers

Scale requirement: practical consequences

Practical consequences

Consolidation

Scale “will help to deliver lower investment fees, increased returns and access to diversified investments, as well as better governance and expertise in running schemes”

Baroness Sherlock

Practical consequences

Consolidation

Cost and
complexity

Market
distortion

“Whilst we acknowledge the benefits of scale and support the overall direction of the reforms, we are already seeing market effects of the scale test which are detrimental to member outcomes. **Employee Benefit Consultants (EBCs) are taking smaller schemes off their lists of recommendations to employers where they think the provider may not reach the £25bn AUM threshold (or the transition pathway), making it harder for them to reach scale. In some cases, these smaller schemes offer exceptional, market-leading value for money.**”

Pensions UK

Practical consequences

Consolidation

Cost and
complexity

Market
distortion

Barriers to
entry

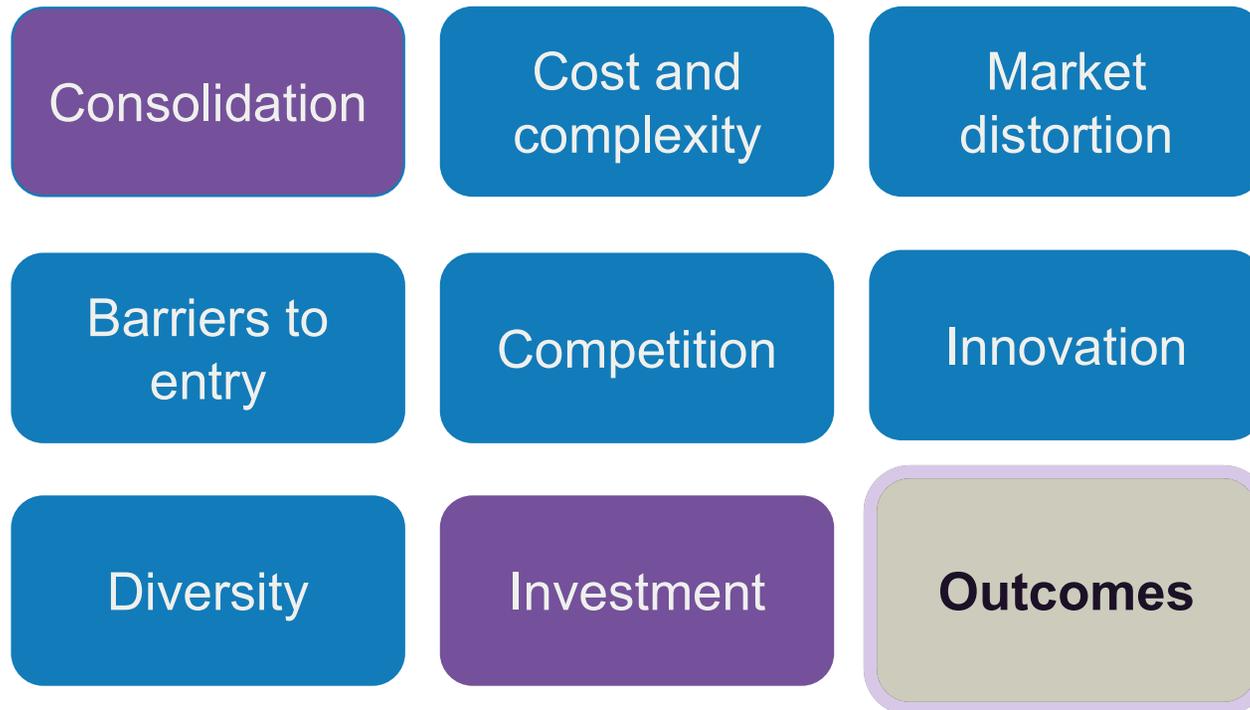
Competition

Innovation

"Inherent to most of the innovation in the market – for example, in collective defined-contribution schemes – is that they would have to operate at scale to be effective."

DWP consultation, Retirement Collective Defined Contribution pension schemes

Practical consequences



Asset allocation: practical consequences

Pension pots of savers at risk from new UK rule, industry experts warn

Forcing defined contribution schemes to invest a minimum amount in private assets could 'lead to poorer returns'



Jeremy Warner

Here's a great idea for making Britain's pensions disaster even worse

Forcing people to put their savings into the UK stock market is a repudiation of basic market economics

The government wants to consolidate Britain's fragmented pension system and kick-start growth by encouraging more domestic investment by UK funds © Rosemary Roberts/Alamy

"As such, we urge you to be bold. Condition the privileges that are granted to UK DC pension scheme default funds upon them allocating a minimum 25% of their default fund assets to UK investments - across each asset class. This is not mandation as individuals could choose to opt out of the default fund without losing any of their pension entitlements."

Letter from David Schwimmer (London Stock Exchange Group) and others to Rachel Reeves

"Pensions UK **does not support** the introduction of a reserve power to allow Government to direct how DC schemes invest. We understand the Government has said it does not intend to use the power so long as the Mansion House Accord targets are met."

"However, crucially, this ambition is subject to **fiduciary duties** and is dependent on **supporting actions by Government**, namely that there will need to be a strong pipeline of investable UK assets. Without this, schemes will be competing against each other for the same assets, which risks **asset bubbles and poor value for money.**"

Pensions UK

“This power raises more questions than it answers - for example **who is legally accountable** for underperformance and how will the assets that are within scope be determined. It will also have a negative effect on market pricing and could **undermine public trust** given scheme members, or those thinking of saving in a pension, may worry that **saver returns are no longer the main priority**. There are arguments to either mandate or not mandate but having the mere threat of mandation is widely viewed as **the worst of both worlds.**”

Society of Pension Professionals

Competing duties

- “***best financial interests***” – Cowan v Scargill
- Regulator may exempt if “meeting the asset allocation requirement would cause ***material financial detriment to members*** of the scheme” – Pension Schemes Bill

Legal consequences

Legal issues

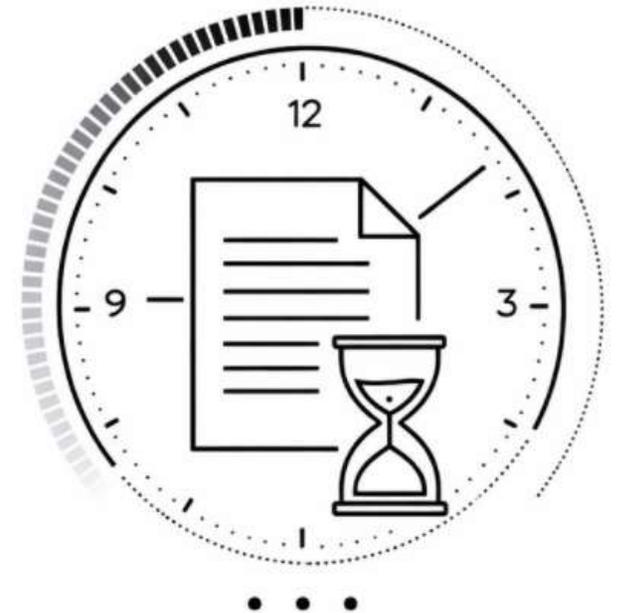
Competing
duties

Uncertainty

Compliance

Some final thoughts

- Underlying regulations yet to be published
- Practical steps to prepare, member communication
- Scale likely to be a good thing
- Regulation vs market forces



Questions