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Dear Keir and Tommy,

When we debated Part 2 of the Pension Schemes Bill on Wednesday 7 January 2015, I said I would provide more detail on our intentions around the consultation and other discussions that will help us frame our regulations.

Consultation process and provisional timetable for regulations

We do intend to have a full and open formal consultation on draft regulations, to be made under powers contained within Part 2 of the Bill, which set out the governance and other requirements that schemes providing collective benefits will need to adhere to – but we want to do more than that. Unlike the measures relating to the pension flexibilities that will come into effect in April 2015, the regulations for Defined Ambition and collectives do not need to come into effect until later, and not before 2016. Therefore, before formally consulting, we plan to build upon the work we have already done and to continue to talk with employers, providers, actuaries, unions and consumer groups to establish how best to frame the detailed regulatory requirements for schemes that offer collective benefits.

Some of these meetings are already in the diary, and they will allow officials to work through the Spring with a view to providing key draft regulations for a full and open public consultation later this year, aiming to bring key regulations in for April 2016.

We will need to review the timetable, following changes to the Bill (which we intend to table at Lords' Report) in response to the recommendations of the Delegated Powers and Regulatory Reform Committee, meaning some of the powers contained within Part 2 of the Bill will be subject to the affirmative procedure on first use. This will bring some additional challenges to the timetable. However, it is important that we respond to the appetite we know exists with development of the secondary legislation. The best way of doing that is to develop the provisions, working with those that might deliver the schemes.

Regulatory powers within Part 2 of the Bill

As I mentioned during the Committee stage, our default position is that we will lay regulations against each power that we have taken in Part 2 of the Bill. The drafting intentionally refers to both trustees and managers; as collective benefits can be provided by both occupational and personal pension schemes, whether they are trust or non-trust based. The regulation-making powers are therefore capable of being used to impose requirements on personal and contract-based schemes offering collective benefits.

However, further discussions between Government and the Financial Conduct Authority (FCA) are needed to establish precisely how regulation of different types of schemes providing collective benefits would work best in practice. We will work closely together to make sure that rules and regulations deliver consistent protections for members regardless of whether the requirements on schemes are set out in regulations made under Part 2 of the Bill or in FCA rules. It may be, for instance, that whilst it would be appropriate for regulations made under powers contained within Part 2 of the Bill to apply to occupational pension schemes, FCA rules should set out the requirements for personal pension schemes offering collective benefits.

This does have implications for the wording of the regulation-making powers contained within Part 2 of the Bill. In particular, a large number of the powers provide that the Secretary of State 'may' (rather than "must") make regulations which require trustees or managers of a pension scheme to draw up and follow certain documents, or to act in a particular manner.

If regulation of personal pension schemes would most appropriately be governed by FCA rules, then we would not want the Secretary of State to be under a duty to make regulations for those schemes as well. This would either mean duplicate provision with consequent expense for schemes and members, or potentially leave the Secretary of State in breach of a legal duty. In conclusion, as I said in the debate, the Government's clear intention is to ensure that the schemes are appropriately regulated in relation to the matters set out in Part 2 of the Bill. What this means is that, for example, there will be requirements on schemes to set targets, have policies on factors used to calculate benefits, on how to deal with deficits and surpluses, and how to calculate transfer values etc. These requirements may be set out under the regulation making powers in Part 2 for occupational and personal pension schemes, or they may be set out in FCA rules in relation to personal pension schemes, and in regulations made under powers contained in Part 2 of the Bill for occupational pension schemes.

Our view is therefore that, as currently provided in Part 2 of the Bill, it is more appropriate to have permissive rather than mandatory powers to set out these requirements where needed..

Placing a fiduciary duty on managers

In addition, to ensure that members' interests are appropriately protected, Clause 37 in Part 3 includes a power to enable us to require that managers of non-trust based

schemes act in the best interests of members when making certain decisions.

This provision ensures that we have the ability, if required to provide additional member protections where managers are making certain decisions specified in regulations. This reflects the different types of decisions and risks that occur in certain DA schemes and in respect of collective benefits.

As with other provisions in part 2 our aim is to deliver consistent protections for members regardless of whether they are in a trust based or non-trust based schemes in respect of certain member risks. Trustees will already be required to act in the best interests of members due to their fiduciary duty.

However, at this stage we do not want to pre-judge whether regulations under Clause 37 requiring managers of non-trust based schemes to act in the best interests of members when taking specified decisions will be necessary. There are important issues we want to discuss further with member representative groups, industry and regulators before we can reach a view. FCA rules may present the best way forward, in which case we want to avoid dual recognition.

I want to assure you that we have taken this power to make sure that we can protect members in non-trust based schemes if needed, and to ensure parity in regulation between shared risk schemes and schemes offering collective benefits whether trust-based or non-trust based. We need to take account of interactions between FCA requirements and any regulations we make, and this may change over time as either pension schemes change, or the way they are regulated by the FCA changes. This means it may be the case that the appropriate protection can be put in place completely through FCA requirements, either now or in the future, meaning regulations under Clause 37 would not be required. However, we cannot be sure the FCA requirements on their own will always achieve what we want, which is why inclusion of the power in the Bill is necessary.

We have therefore taken the power in Clause 37 so we can make regulations to provide protection to members in non-trust based schemes if that is necessary. However, notwithstanding our commitment to ensure protections are in place, for the reasons set out above, we do not believe that it would be appropriate to require the Secretary of State to exercise the power to regulate and we have therefore drafted the Clause using the word "may" rather than "must".

Collective benefits: annual review

We also discussed your amendment which would have subjected the provisions of Part 2 to a mandatory annual review. Further to what I said in response to your amendment, I would like to explain some of the other issues that arise because of timing.

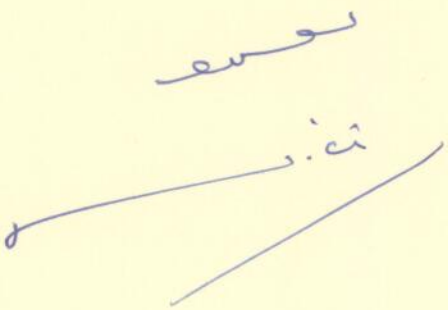
As I have mentioned, we aim to have key regulations in place in April 2016, with guidance etc. from the regulators to follow from that. We want to monitor closely developments in this area, and will want to identify quickly any issues that arise that prevent schemes starting up or operating appropriately. But we recognise that

there will be a need for a degree of bedding down.

Also, with the best will in the world, there is a degree of uncertainty about the timing as we go forward, and so a fixed timescale for reviewing collective benefits might be unhelpful. Review too early and schemes will not have time to be set up, too late and we may miss issues that should have been picked up earlier.

We would therefore want to review and report at the right time following the secondary legislation being in place. This is likely to be three years after we have provided the complete framework to schemes. I hope you agree that a requirement in primary legislation for an annual review of collective benefits may be inappropriate, but I am happy to give an undertaking that we would conduct such a review three years after the main set of regulations governing the operation of collective benefits come into force, and report back to Parliament with our findings and conclusions.

I hope this helpfully explains our position on these important issues and helps inform the further debates on the Bill. I have placed a copy of this letter in the Library and I am copying it to all Peers who spoke during Committee.



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The Right Honourable Lord Bradley and
The Right Honourable Lord McAvoy
House of Lords