



Department
for Work &
Pensions

Consultation Questions: Facilitating Investment in Illiquid Assets

Name of respondent(s)/organisation (please provide):

Matthew Levine (matthew.levine@actuaries.org.uk) – Institute and Faculty of Actuaries

Pension Scheme type (cross all those that apply)

Master Trust (500+ employers approx.): ...

Master Trust (fewer than 500):

Single-employer trust:

Contract-based:.....

Defined Benefit:.....

Hybrid:.....

Administration:

Investment consultant:

Consumer organisation:

Law firm:.....

Other (please state):.....

Please indicate, next to any responses given, if you are **not** content for DWP to publish relevant sections of your responses in the future. Without a specific request for anonymity, we reserve the right to publish your response in full.

Chapter 2: Introducing Disclose and Explain Policy Proposals

Question 1: Do you support these proposals and agree with the government's rationale for intervention?

1. We support the Government's aim to broaden the factors which members, employers and consultants are able to use in comparing schemes. We agree that including schemes' policies and (where applicable) asset allocations on illiquid investments within such comparisons will create a more robust assessment of value for money.
2. As the consultation paper notes (paragraph 80) there are also barriers to illiquid investment that trustees are not in a position to address, such as the systems on which providers run DC pension funds. These are often set up for daily pricing and dealing even though this is not required by pension funds and is unhelpful for the management of illiquids (where prices are usually stale, therefore).
3. We think the Government should provide more detailed justification for separating out infrastructure investment, and more detailed guidance on how to do this consistently, since this could take the form of either public or private equity or public or private debt, as well as, for a few larger schemes, a directly-owned piece of real estate.
4. We believe the proposals could say more about the key messages that could help members as a result of disclosing illiquid investments. These might include:
 - a) That ongoing pricing of the DC fund's units may be affected (since the illiquid components may be priced infrequently);
 - b) That the liquidity of the DC fund itself might be affected;
 - c) That the returns achieved by the DC fund might be affected (hopefully positively in the long term).
5. Similarly, any statement by larger schemes of asset allocation to illiquids ought to be accompanied by an opinion from the trustees about the purpose of these investments, e.g. that they do (or do not) expect this level of illiquid investment to prevent their units from being readily realisable or switchable.
6. Turning to the mechanics of these proposals, we are not clear why the SIP amendment is needed in law rather than in guidance, since the law already requires the topics around illiquids to be discussed. We also think the proposed disclosures will not integrate into the overall narrative of the SIP as effectively as similar proposals for ESG and climate change did.

Question 2: Do you agree with the scope of this proposal?

7. The proposal to disclose and explain their policies on illiquid investments in the SIP would only apply to the default arrangements of occupational DC schemes. Illiquid investment is appropriate for default vehicles, where changing exposures are managed for members over their lifetime. We agree that trustees' policy on this could usefully be disclosed in the SIP.

8. It seems reasonable that DC 'self-select' funds, where members do not have the benefit of this management, are excluded from the proposals.
9. The paper explains that DB schemes would be excluded because they now typically have shorter term investment horizons. However, managing liquidity arguably becomes more important as DB funds mature, and we would also note that the majority of pension fund assets are still in DB funds. We would therefore suggest considering whether they too should be subject to the disclosure proposals.

Question 3: Considering the policy objective, to require trustees to state a policy on investment in illiquids, how should we define "illiquid assets"?

10. We would firstly say that by focusing on definitions in this question there is a risk of detracting from the central objectives that investing in illiquids are intended to achieve. For example, an open letter from the Prime Minister and the Chancellor to institutional investors in August 2021 mentioned building back better, a green revolution and scientific innovation as key elements in an 'investment big bang'.¹
11. There is a reference in the discussion following the definitions (paragraph 92) to a listed investment company. It is important not to equate "listed" with "liquid", since factors like the size of investor depth, analyst coverage and at times market sentiment could make a listed investment illiquid. Similarly an unlisted asset – such as cash – can be liquid.
12. Turning to the two proposed definitions, Option 2 is a 'look through' approach which would focus on asset classes considered illiquid. This seems like a transparent approach.
13. Option 1 measures the proportion of illiquid assets in a given fund, in order to classify the fund as a whole as liquid or illiquid. To do this consistently would require an unambiguous definition of which assets to class as illiquid.
14. Under Option 1, scheme A could hold just one fund deemed illiquid, compared with scheme B holding many funds with illiquid assets but not enough to make the funds themselves count as illiquid. Scheme B could have a much larger underlying allocation overall, but this wouldn't come across in its disclosures.

Question 4: Do you agree with the proposed aspects of a scheme's illiquid asset policy that we would require to be disclosed and timing of such disclosures?

15. Although the proposed disclosures are quite limited in length, we would still question the need to disclose all the details listed in paragraph 98, and we would welcome more explanation on how the information is intended to be used.

¹ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1008814/A_Challenge_Letter_from_the_Prime_Minister_and_Chancellor_to_institution_1.pdf

16. On timing of disclosures, we would welcome clarification that a decision to begin investing in illiquid assets would count as a significant change in investment policy for the purposes of this disclosure.
17. It is proposed that the SIP should mention what illiquid assets are. We think it would be more appropriate for the government to provide wording here. This would ensure consistency and avoid placing the burden on trustees to define illiquid assets.
18. The consultation proposes that schemes should describe different members' allocations to illiquid assets, including whether the investments are direct or indirect. However, if illiquid assets are defined using Option 2 of Question 3, which focuses on the underlying asset classes, it would not be necessary to know if investment was direct or indirect.

Question 5: Do you agree that with the proposed level of granularity for this disclosure? Are the asset classes and sub-asset classes proposed in the example above appropriate for this kind of asset allocation disclosure?

19. We agree that information already widely available should be required, which will make it easier for members to compare schemes. We also agree with the government's approach to provide more detailed guidance about the manner of disclosure, but not to hard-code this in regulations so that trustees have the freedom to take account of their members' specific communication preferences.
20. The seven proposed asset classes could be extended to include e.g. derivatives and hedge funds.
21. Depending on the approach to defining illiquid assets discussed in Q3, it would be helpful to include more detail on how a look-through approach would work where schemes delegate asset allocation using multi-asset funds.

Question 6: Do you agree that holding £100 million or more of total assets in an appropriate threshold for determining which DC schemes should be required to disclose asset allocation?

22. We believe that a threshold is unnecessary and that it would be reasonable to apply the disclosure requirements to all schemes. For some smaller schemes that struggle to comply, the disclosures could act as a trigger towards the government's goal of greater consolidation.
23. We would welcome more clarity on why total scheme assets are used to determine the threshold for disclosing, whereas the disclosure requirements themselves apply to the DC default fund. For example, this would seem to imply that a £100m hybrid scheme with mostly DB funds, or a £100m DC scheme with significant self-select assets, would be subject to the requirements even if their default funds were small.

Question 7: Do you agree that we should align the disclosures with the net returns' disclosure requirement?

24. Although the consultation proposes alignment with net returns it also suggests that a 'years to retirement' approach could be used instead. We would suggest allowing schemes to choose which method suits them better.

Question 8: Do you agree with the frequency and location of the proposed asset allocation disclosures?

25. It makes sense to disclose asset allocation information alongside other requirements in the Chair's Statement, and therefore annual disclosure seems appropriate.
26. We believe that disclosing the starting and ending allocations with a verbal description of asset allocation changes throughout the year would be a more meaningful approach than using the average allocation at four valuation points throughout the year.

Question 9: Please provide estimates of any new financial costs that could arise from the proposed "disclose and explain" requirements. Please outline any one-off and ongoing costs.

N/A

Chapter 3: Employer-related investments – Consultation on draft regulations

Question 10: Do you think the current regulations relating to ERI in the 2005 Regulations present a barrier to Master Trusts expanding investment strategies to include private debt/credit?

(Please enter your response here)

Question 11: Do the draft regulations achieve our policy intent?

(Please enter your response here)

Question 12: Do you agree with the information presented in the impact assessment?

(Please enter your response here)