Facilitating investment in illiquid assets

Isio response to consultation on proposals to improve the accessibility of illiquid assets for defined contribution pension schemes

isio.

Isio view

We are very supportive of using illiquid assets in defined contribution (DC) scheme strategies, and investment from large schemes and master trusts will be crucial to overcoming the challenges currently faced by the industry. The latest disclose and explain proposal is a good example of looking outside of just the charge cap, but we are wary of the ever-growing governance burden which trustees face.

This consultation follows on from the government's 'Enabling Investment in Productive Finance' (charge cap reform) consultation. Isio's response to that consultation can be found on our website: Enabling investment in productive finance (isio.com)

Meet the experts

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Consultation questions

Question one

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

Isio response

As noted in our previous consultation response, Isio are very supportive of the case for illiquid investment in DC. We believe there is a strong investment case as it will lead to better outcomes for members and improve long-term risk adjusted returns.

Isio are also supportive of the DWP's proposal which looks more broadly than just removing performance-related fees from the charge cap, as we believe there are other structural factors which hinder the ability for DC schemes to access illiquid investments. We are pleased to see the DWP take a more radical approach to solving this problem, and we believe investment from large schemes and master trusts will be crucial to overcoming the challenges currently faced by the industry.

We note that the proposed approach has been successful in other areas, such as ESG, where disclosures have encouraged schemes to review their approach and this has coincided with significant improvements in how pension schemes incorporate ESG into their investment strategy.

Question two

Do you agree with the scope of this proposal?

Isio response

We are comfortable with the proposed scope of applying the disclosure requirements to DC defaults only, as this is where the vast majority of DC members are invested. Isio agree that DB schemes have been accessing illiquids for a long time, and there are fewer structural issues in that area of the market.

We also acknowledge that the much lower take up and less certainty on member cashflows impacts the ability of fund managers and platform providers to offer illiquid investments as self-select options.

Question three

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

Isio response

In order to truly capture illiquid investments and help resolve some of the issues around DC schemes accessing these funds, Isio would prefer to define illiquids on a look through basis where the underlying investments are "assets that are not able to be sold without a significant notice period". This would exclude listed property funds, for example, which we do not feel offer true illiquid characteristics as performance is often more correlated with listed equities than the underlying asset.

In addition, if a DC scheme uses a daily dealing multi-asset fund which invests in some underlying illiquid assets, we believe this should be recognised as providing true illiquid exposure. Therefore we are more aligned with your definition 2, and doing a look through to the underlying assets to assess liquidity at an underlying asset level.

Question four

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?

Isio response

Isio believe it would be beneficial to also include a formal date for compliance to ensure that this is addressed by all schemes after the legislation is introduced. We have found that the required date for previous SIP updates (e.g. 1 October) was a helpful prompt for all schemes to review.

We note that given the increasing list of SIP requirements, Isio believe it would be helpful to prepare a simple checklist detailing all policies that must be included in the SIP, so schemes can ensure they remain compliant.

Once a scheme's illiquid asset policy is in place, we agree with the proposal that it is then reviewed in line with the SIP, at least every 3 years or more frequently after a strategy change.

Question five

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?

Isio response

We see limited rationale for requiring schemes to disclose their asset allocation in the Chair's Statement as this information is already available to members (e.g. in factsheets) and the requirements of the Chair's Statement are already onerous.

We believe more engaged members could find this information out for themselves and take appropriate action if required. Alternatively if DWP is looking for a central point to obtain and collate this data on a consistent basis, then via the annual TPR Scheme Return may be a more suitable place (as is collated for DB schemes).

However, if there is a strong desire to include this then it should be quite light touch and not be excessively onerous for schemes to calculate.

Question six

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?

Isio response

Please see our response to question 5.

Question seven

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

Isio response

Please see our response to question 5. If there is a strong desire to include this information, Isio believe it makes sense to align different member ages and be consistent with the net returns disclosures which are also included in the Chair's Statement.

Question eight

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

Isio response

Isio note the requirement to average over the year creates additional work for trustees to calculate and given the extensive disclosures already required by the Chair's Statement we question whether this is necessary.

Our proposal would be to show at the previous and current reporting year ends only.