

UK pension reform post Mansion House speech



Rachel Reeves, the UK Chancellor of the Exchequer, delivered her first Mansion House speech on the evening of Thursday 14th November 2024.

A key area that she covered was the next phase of UK pension reform. To coincide with the speech, HM Treasury (HMT) and the Department of Work and Pensions (DWP) published their *Pensions Investment Review: interim report, consultations and evidence*.

The publication package consisted of four documents.

- Pensions Investment Review Interim Report
- Pensions Investment Review: Unlocking the UK pensions market for growth
- Pension fund investment and the UK economy
- Local Government Pension Scheme (England and Wales): Fit for the future

These are discussed below

Pensions Investment Review Interim Report

You can find the report [here](#).

It is an update on Phase One of the review. As covered in our newsletter, the terms of reference for phase one were published on 16th August 2024. A Call for Evidence was also published on 4th September and closed on 25th September. You can find the Call for Evidence [here](#).

The Interim Report provides an update on the four workstreams set out in the terms of reference.

Workstream 1

Scale and Consolidation in the Defined Contribution Workplace Market

There is general consensus for the need for scale and consolidation in Defined Contribution (DC) schemes. The report makes it clear that the government sees this applying to a lot more than just the smallest schemes.

Measures designed to achieve this are set out in the consultation paper, *Pensions Investment Review: Unlocking the UK pensions market for growth*, covered below.

The more radical proposals for multi-employer schemes, to introduce minimum size requirements for default funds and to place limits on the number of default funds, would not apply before 2030 at the earliest.

Workstream 2

The Local Government Pension Scheme

The report identifies three areas of focus:

- Consistent approach to asset pooling
- Local investment
- Strengthening governance

Detail is set out in the consultation *Local Government Pension Scheme (England and Wales): Fit for the future* covered below.

Workstream 3

Cost vs Value in the Defined Contribution Workplace Market

A key objective of the Pensions Investment Review is to promote a greater focus on the value provided by workplace DC pension funds rather than their cost. The move to a focus on Value for Money (VFM) has been a work-in-progress for several years. The framework is to be included in the forthcoming Pension Schemes Bill.

Two areas are flagged:

- The role of employers
- The role of consultants and advisers

This covered in chapter 4 of the consultation paper, *Pensions Investment Review: Unlocking the UK pensions market for growth*, covered below.

Workstream 4

UK Investment

The current and previous governments have expressed concern about the lack of domestic investment by UK pension schemes. At this stage the government has decided not to make specific recommendations in relation to UK investment, beyond those outlined for the LGPS above and below relating to local investments. This may be revisited at a later stage.

Pensions Investment Review: Unlocking the UK pensions market for growth

You can find the consultation [here](#).

This covers two broad areas, neither of which is new and for neither of which are the elements covered in the consultation in our opinion particularly key:

- Achieving scale in the Defined Contribution market;
- Costs versus Value: The role of employers and advisers

These are discussed further below.

Achieving scale in the Defined Contribution market

The consultation is on some very specific proposals on minimum size for default funds and provisions for allowing transfers of contract-based schemes. We are not in a position to comment on either point.

More generally, we think that it is good thing that there is no separate, specific plan for consolidation. The rationale for achieving scale is that smaller schemes are felt to

offer poorer outcomes for scheme members. Focus on Value for Money should therefore correctly be the main priority. This is sort of covered below.

Costs versus Value: The role of employers and advisers

The consultation poses some rather conceptual questions about the role and potential increased regulation of employers and advisers in the focus on cost rather than value for money.

The more important provisions will be in the Value for Money (VFM) Framework This is currently being developed by the FCA, TPR and the DWP, so there is nothing available yet to discuss.

The elephant in the room



As we have covered in our newsletter in recent years, there remain significant practical obstacles to investment in illiquid assets by DC schemes, particularly the role of the platforms. Much of the market is not set up to accommodate funds with notice periods. This is a problem for investment in underlying funds investing in illiquid assets. This is not addressed in the consultation. It is not clear when and how the government plans to address this.

There is also a role for the industry in educating those running DC schemes on the long-term merits of investment in real estate as an asset class and how this might be effected in practice. The Association of Real Estate Funds and the Investment Property Forum are currently working on plans for this.

Pension fund investment and the UK economy

This is a general paper analysing the trends of UK pension fund investment and the implications for UK economic growth. You can find it [here](#).

Happy bedtime reading.

Local Government Pension Scheme (England and Wales): Fit for the future

You can find the consultation [here](#).

As mentioned above, the consultation covers three areas of focus:

- Consistent approach to asset pooling
- Local investment
- Strengthening governance

LGPS pooling

The 86 administering authorities (AAs) for the LGPS have already combined, at least theoretically, into eight pools. Progress in actual pooling has been patchy and the consultation conveys the new government's sense of disappointment. The proposals are not a doctrinal change from the reforms initiated by the previous regime, but a call for more vigorous flogging of the recalcitrants.

The consultation sets out a number of specific proposals. Although this is set out as a consultation, the government view on each aspect is made clear:

- AAs would remain responsible for setting an investment strategy for their fund, and would be required to fully delegate the implementation of that strategy to the pool. Crucially for investment managers, investment decisions and selection of managers would be taken away from the AAs to the pools;
- AAs would be required to take principal advice on their investment strategy from the pool;
- Pools would be required to be established as investment management companies authorised and regulated by the FCA, with the expertise and capacity to implement investment strategies;
- AAs would be required to transfer legacy assets to the management of the pool. Although the question is posed, "do you agree that administering authorities should be required to transfer legacy illiquid investments to the management of the pool?", the text suggests that the answer is expected to be "yes". It is also interesting that it refers to the management rather than the ownership;
- Pools would be required to develop the capability to carry out due diligence on local investments and to manage such investments. This refers to the next section of the consultation, covered below.

The expectation is that proposals will be submitted by 1st March 2025 with implementation by March 2026. It will be interesting¹ to see how the pools respond in their proposals, particularly for the consultant and external manager layer.

¹ Much in the way of the apocryphal Chinese curse or the speeches of Joseph Chamberlain

Local investment

This has the potential to be the most controversial area. It is important not to lose sight of the overriding fiduciary duty to the members of the scheme, rather than to the infrastructure priorities of local politicians. However:

- If scheme members want an allocation to investments in their own region, there would not seem to be anything fundamentally wrong with this. This happens already, perhaps just with slightly less structure;
- The consultation recognises the potential challenges and seeks to move the investment process and ultimate decision away from the individual AAs to the pools.

The proposals at this stage are quite general:

- Requirement to set out approach to local investment in the Investment Strategy Statement, which is reviewed every three years;
- Requirement to work with combined authorities and similar bodies. The presumption is that AAs will bring forward proposals so doing nothing would not be an option;
- Requirement for pools to carry out due diligence on potential local investments
- Requirement to report annually on local investment

The government proposes to set out new requirements in regulations, so we wait to see how prescriptive these will be.

Governance of funds and pools

The government wants improved governance at the AA and pool level.

For the individual AAs, the consultation proposes the following:

- Requirement to prepare a governance and training strategy
- Requirement to identify a senior LGPS officer
- Requirement to prepare an administration strategy
- Improving readability of annual reports
- Requirement to participate in a biennial independent governance review
- Requirements on knowledge and skills for those involved in the management of LGPS funds
- Requirement for pension committees to appoint an independent person who is a pensions professional, whether as a voting member of the pensions committee or as an adviser.

For the pools, the consultation proposes the following:

- Pool boards to include a representative or representatives of the group of partner AAs
- Requirement for pools to publish asset performance and transaction costs

Conclusion

- There is nothing fundamentally new in the proposals. For both the LGPS and DC schemes, the new government seeks to increase the pace of implementation of steps initiated by the previous government;
- The detail will be in legislation and other proposals that are yet to be published;
- The elephant is still very much in the room with respect to practical implementation.

We will continue to feed into consultation responses via the Association of Real Estate Funds (AREF) Pensions Reform Working Group and to provide updates in our newsletter.

17th November 2024