Invested in a better future

Pensions Policy
Financial Conduct Authority
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Dear Pensions Policy Team,

Pensions: Adapting our requirements for a changing market

The BVCA is the industry body and public policy advocate for the private equity and venture capital (private capital) industry in the UK. With a membership of over 600 firms, we represent the vast majority of UK-based private capital firms, as well as their professional advisers and investors. In 2023, £20.1bn was invested by private capital into UK businesses in sectors across the UK economy, ranging from consumer products to emerging technology. There are over 12,000 UK companies backed by private capital which currently employ over 2.2 million people in the UK. Over 55% of the businesses backed are outside of London and 90% of the businesses receiving investment are small and medium-sized businesses.

We welcome the opportunity to provide feedback on this Discussion Paper, which we note refers to the FCA's willingness to consider further rule changes that might support the wider UK growth agenda. Below we have set out two specific areas in which the BVCA believes there is a strong case for changes to existing rules.

1. Further changes to the 'permitted links' rules are needed to support productive investment by DC

The Discussion Paper invites views (para 1.7) on how the FCA can support productive investments by UK pensions, and welcomes comments in particular on what more could be done in relation to the permitted links rules.

The Pensions and Private Capital Expert Panel, convened by the BVCA in partnership with the ABI and the PLSA, has published an interim report identifying further such changes that the FCA could make to the permitted links rules in order to facilitate access to private capital funds for DC schemes that invest through insurance platforms. The Expert Panel is comprised of senior leaders from both the pensions and private capital industries with a remit to explore how UK DC pension investment into UK private capital funds can be facilitated, in line with the Mansion House Compact.

The LTAF framework has offered a route for DC schemes using life insurance platforms to invest more easily in illiquid assets. However, this route complicates the market infrastructure for DC investment in private capital by inserting an intermediate vehicle between DC schemes and underlying private capital funds, which brings additional administration costs and liquidity requirements that cause a 'drag' on DC investors' returns, relative to investing in private capital funds directly.

These additional costs are not suffered by DC schemes that do not invest through life platforms, despite both types of scheme being professionally managed and having underlying beneficiaries with the same profile. This is because non-life schemes are not subject to the permitted links rules and so do not have to establish LTAFs to access illiquid assets. This is why the LTAFs that have been established so far are overwhelmingly targeted at DC schemes investing via life platforms, whilst non-life platform schemes have not typically invested through LTAFs. This means there is an unlevel playing field between different types of DC schemes, which the BVCA, building on the conclusions of the Expert Panel, believes should be rectified by amending the permitted links rules. We think there are two options for doing this:

- **Excluding the default funds of DC schemes from the 'permitted links' rules:**

  From a broader policy perspective, the Expert Panel believed this change would be appropriate because DC schemes are professionally managed by trustees, and with a legal obligation to seek professional investment advice (i.e. they are not retail funds). This would also ensure a level playing field with DB schemes and DC schemes that do not invest through life insurance platforms, which are not subject to such restrictions. This could result in a wider range of private capital investment options being made available to DC schemes via platforms.

- **Including certain private capital funds explicitly as conditional permitted links and exempting them from the 35% cap on illiquid assets:**
  As an alternative, the permitted links rules could be amended to treat other commonly used private capital investment vehicles in the same way as LTAFs are treated under the rules. Private capital firms already offer a range of semi-liquid, regulated vehicles (principally for the wealth management market) whose inclusion as conditional permitted links would seem to be a natural extension to including the LTAF. The criteria for this approach to a particular type of vehicle would need to be developed further. One consideration to explore might be whether a candidate vehicle for explicit inclusion is subject to product regulation in another jurisdiction (such as European Long Term Investment Fund and Luxembourg's "UCI Part 2" offering).

2. Application of the DC charge cap to FCA-regulated schemes

The BVCA welcomed DWP's changes to the Occupational Pension Schemes (Charges and Governance) Regulations 2015, which enable some performance-based fees to be excluded from the definition of 'charges' in default arrangement charge cap calculations in the trust-based environment.

However, this change applies only to the trust-based market, and the equivalent change has not been made to FCA rules, to enable contract-based DC schemes to exclude performance-related fees. At the moment COBS 19.6.6R limits all administration charges to 0.75%. This causes additional complexities for providers with a default investment strategy that is used by both master trusts and contract-based DC clients. It also restricts access to a more diverse investment strategy according to the legal structure of the scheme.

We understand that this impacts a number of providers, and is proving to be another barrier to implementing private market investment for those providers. Given the equivalent change has already taken effect in the trust-based market, and in light of the FCA's wider work around Value for Money in contract-based DC pensions, the BVCA believes the same change needs to be made to the FCA framework.

We would welcome the opportunity to discuss both of these proposals in further detail.

Please do not hesitate to get in touch if you have any questions or if you would like to discuss any of the above in more detail (please contact Tom Taylor ttaylor@bvca.co.uk / Karen Hurst khurst@bvca.co.uk).

Yours sincerely

Tom Taylor,

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