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By: Connor Hussey
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NEWS & ANALYSIS

Partners Group: 'Great deal of interest' in 401(k) market

2021 marks the year products aimed at tapping the defined contribution market see the light of day. Increased interest in such vehicles suggests more are soon to come.

Department of Labor guidance last year sparked a push by managers to create products that can access the vast pool of capital in defined contribution plans like 401(k)s. An executive at one of the firms offering such products, Partners Group, said this year could see a bevy of further offerings.

"We are now, with that letter [from the DoL], observing a great deal of interest across the landscape," Robert Collins, head of Partners Group's US distribution business told sister publication Private Funds CFO. "We know that there are a number of new managers that are developing products, we know that there are managers that are developing products with the goal of launching those this year. We also know that pensions and consultants are engaged on the topic with renewed vigour, as are asset managers who manage traditional target-date funds."

Partners Group and Pantheon had sought guidance from the DoL since at least 2017, and were both instrumental in its release last summer. Both firms have been developing collective investment trusts for this sole purpose. CITs are


Robert Collins

commonly used in public markets for allocating 401(k) funds to public investments but are not as popular among PE managers when compared with the cheaper '40 Act' fund option.

But in order for the market to really get off the ground, more private markets competition is needed.

"I think the competition will fuel this market," said Josh Lichtenstein, Employee Retirement Income Security Act partner at Ropes & Gray. "The more credible products a plan sponsor can compare, the more likely it is to see plan sponsors adopting these products in greater numbers."

Competition in the form of CITs is expected to begin later this year, although the regime change in Washington, leaving the Democrats in control of Congress and the White House, has some leaders worried about the future for the inclusion of retail money in private investments.

Collins batted down that concern, at least as it applies to the DoL's guidance: "We continue to believe it would be extremely unusual and unexpected for the letter to be retracted as it is, in essence, a restatement of long-held department beliefs."

President Biden's pick to head up the new DoL, Boston mayor Marty Walsh, still awaits Senate confirmation. But his experience as a member and longtime president of the Laborers' Union in Boston – whose allocations include private equity, real estate and even hedge funds – is reassuring to those hoping progress for PE's access to retail money will continue.

And a recent court decision seems to support the legitimacy of 401(k) plans investing in private equity.

Intel decision

At the end of January, a US District Court judge dismissed claims by two former participants in two of tech giant Intel's defined contribution plans that fiduciaries violated their ERISA obligations by allocating to private equity and hedge funds.

The plaintiffs argued that Intel's decision to allocate to these investments subjected participants' retirement to considerable risk for comparatively high fees and poor results, and that Intel fiduciaries "drastically departed from prevailing standards of professional asset managers", according to the plaintiffs' original complaint.

"Although plaintiffs allege comparisons of the Intel funds' performance to 'peer' and 'comparable' funds, plaintiffs have failed to provide sufficient allegations to support their claim that these other funds are adequate benchmarks against which to compare the Intel funds," said US District Court judge Lucy Koh in her 21 January opinion.

"Simply labelling funds as 'comparable or 'a peer' is insufficient to establish that those funds are meaningful benchmarks against which to compare the performance of the Intel funds," she added.

Judge Koh also noted that ERISA "does not require that fiduciaries mimic the industry standard when making investments."

The 401(k) market is rife with litigation, Lichtenstein said, compared with the defined benefit plan market, which already allocates significant capital to private equity. Despite the supportive Intel decision, that litigiousness might yet impede the wider integration of 401(k) money into the market. "But it also just points to the fact that the more this market develops, the more plan sponsors are adopting these products, the more confident people are going to feel about the litigation risk and the more we'll see this take off." ■