abrdn plc – Written evidence (SCG0008)

About abrdn

• abrdn is a global investment company that helps clients and customers plan, save and invest for the future. Our purpose is to enable our clients to be better investors.

• abrdn manages and administers £505.9bn of assets for clients (as at 30 June 2024).

• Our strategy is to deliver client-led growth. We are structured around three businesses – Investments, Adviser and interactive investor – focused on the changing needs of our clients.

• The capabilities in our Investments business are built on the strength of our insight – generated from wide-ranging research, worldwide investment expertise and local market knowledge.

• Our Adviser business provides financial planning solutions and technology for UK financial advisers, enabling them to create value for their businesses and their clients.

• interactive investor (ii) is the UK's second largest direct-to-consumer investment platform and number one flat fee provider. ii enables individuals in the UK to plan, save and invest in the way that works for them.

Executive summary

The UK is one the great financial centres of the world but this status cannot be taken for granted. As a global investment manager dedicated to supporting our clients around the world abrdn is acutely aware of the competitive threat facing the UK from established and emerging rivals.

To stay ahead in an intensely competitive sector of the global economy will mean embracing and responding to the risks and opportunities created by economic cycles, geopolitics, regional conflict, technological progress, aging populations and a progressive transfer of responsibility for financial security to the individual. These are significant challenges which can only be met in a policy environment based on clear strategic objectives while enabling the financial sector to innovate, adapt and respond to evolving market pressures and requirements.

The secondary objective for international competitiveness of the economy and medium to long-term growth given to the FCA and PRA under the 2023 Financial Services and Markets Act represents an important and welcome step towards creating such an environment.

We have provided responses to the committee’s specific questions below but would emphasise several key points:

- The existing primary objectives of the regulator are themselves contributors to long-term economic growth – helping to support financial stability and investor confidence.
- We recognise that many of the levers for economic growth are not in the hands of the regulators – and it is likely to be very difficult to assess the precise economic impact of individual regulatory policy interventions.
- Regulators must facilitate and support a shift away from a “no risk” approach to policy making. An appropriate level of managed risk is an essential element of thriving capital markets and a thriving economy.
- Alongside an acceptance that adoption of risk is essential to the UK’s future competitiveness and growth, there needs to be a much greater focus on value over cost. An excessive focus on delivering products and service at the lowest possible cost may actually work against the interests of the consumer if it denies access to assets which have higher entry costs but can offer a higher rate of return.
- The UK should ensure its regulatory framework is agile and can adapt in the face of rapid change, moving towards outcomes-focussed requirements.
- International competitiveness cannot necessarily be advanced by significant divergence from international standards. On the contrary, the success of the UK as a global financial services centre depends on maintaining the ability of firms to do business overseas without having to overcome regulatory barriers and other unnecessary hurdles.
- While we welcome efforts to simplify the Rulebook it is equally important that proposals for new/additional regulation are carefully considered, particularly where it may lead to duplication or an overlay of existing rules.

abrdn welcomes the new requirement for the UK regulators to consider international competitiveness and economic as part of their remit. If applied correctly the secondary objective has the potential to foster a more balanced regulatory attitude towards risk which could, in turn, unlock much needed investment for the UK economy. However, the secondary objective must not be used as justification for significant regulatory divergence or weakening of high-level standards which could only serve to reduce confidence in UK markets and weaken the position of the UK as a global financial centre.

Questions

1. What opportunities or changes should be prioritised in order for the regulators to meet their secondary growth and competitiveness objectives effectively?

The G20 Summit in Pittsburgh in 2009 signalled a wave of new regulations and more intrusive supervision by national regulators which has continued to this day. One of the lessons of the last 15 years is that well-designed regulations build confidence and resilience in financial services whereas badly designed regulations do not. In our experience as a global investment company the FCA generally compares better than its peers in this regard and there are tangible initiatives where the FCA is demonstrating its appreciation for better designed regulation (such as DP23/2 for improving asset management regulation). However, given how rulebooks have grown over the years, the increasing business cost of regulatory complexity and the continuing challenge of regulatory fragmentation for firms that operate globally, we would urge the FCA to be unrelenting in its ambition to improve regulatory design across its Handbook.

Further, we believe that much could be done to improve the way in which financial services policy is conceived, developed and implemented to deliver better outcomes. This is particularly true of regulation which applies to almost every aspect of how we help our customers and clients to plan, save and invest for the future.[1]

As regards economic growth, we agree with the view of the Investment Association that perhaps the biggest change required in the current UK regulatory environment is a cultural shift towards accepting risk an integral part of delivering long-term growth. Since the Financial Crisis of 2008 the approach to regulation has tilted toward eliminating risk altogether. There are encouraging signs that this is changing: the FCA's recent reforms to the listings regime explicitly said that the reforms involved a transfer of risk to investors but there is a long way to go in convincing politicians, regulators, the industry, the media, and individuals that an appropriate level of risk is an essential element of thriving capital markets and a thriving economy.[2]

More broadly, recent speeches from FCA leaders are now openly addressing the need to rethink attitudes towards risk and a recognition that a no-risk approach has associated costs to growth and investment. We will follow closely how these sentiments are put into practice.[3]

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[1] abrdn response to Labour's 'Financing Growth' review (December 2023)

[2] UK CAPITAL MARKETS: A NEW SENSE OF URGENCY – co-sponsored by abrdn September 2023

We have been vocal, along with the wider industry, on the need to unlock new sources of private capital to invest in UK assets through public and private markets This includes measures which would facilitate increased allocation of Defined Contribution funds to assets which carry a higher degree of investment risk but also offer better long-term returns. This will require a greater willingness to embrace risk, but it is equally important to acknowledge that returns on such investments need to be assessed on the value they can deliver, not simply the cost. While it may be superficially attractive to keep charges and costs to an absolute minimum, this may work against the interests of the consumer if it prevents access to asset classes and investment which have the potential to offer stronger returns in the long run (in other words, the cheapest option does not always equal best value).

As well as unlocking the potential for UK pension schemes we are of the view that the same can be achieved for retail consumers. Recent studies[4] have highlighted that individuals are missing out on an opportunity to earn better returns over the long term, with the FCA's Financial Lives Survey finding that 4.2 million people in the UK hold more than £10,000 in *cash* which could deliver better outcomes by being invested.

2. To what extent are the regulators focused on the objective to promote international competitiveness and growth? Are there areas where the ability of the regulators to fulfil their secondary objectives might be constrained by having to fulfil their primary objectives?

The FCA's primary objectives help to support orderly and stable financial markets and support consumer and investor confidence, which abrdn believes are of clear benefit to the UK economy in the medium-long term, and which help to make the UK an attractive place to do business. In this sense the primary objectives are aligned to international competitiveness and economic growth.

Whilst the FCA has formally incorporated considerations of the secondary objective into its formal consultative process for regulatory change, there are opportunities to improve analysis and metrics used to inform the regulator's view (see Q8).

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[3] Delivering vibrant capital markets | FCA (8 October – Ashle Adler, FCA Chair); Predictable volatility | FCA (8 October – Nikhil Rathi, FCA Chief Executive); Like London's Roman Wall, financial rules must adapt | FCA (24 September 2024 – Sarah Pritchard, FCA Executive Director, Markets and International); Catalysing productivity and growth: A change in mindset on financial inclusion | FCA (19 September 2024, Nikhil Rathi, FCA Chief Executive)

[4] Barclays – The UK Investment Gap, September 2024

There can also be a potential for conflict where, in pursuit of its primary objectives, UK regulators adopt rules which diverge from those in other international jurisdictions. This may happen for a range of reasons: (i) the rules in other international jurisdictions are less well-designed than those of the UK, (ii) the complexity of policy development and implementation or (iii) rules designed or adapted to the specifics of their local markets.

Regardless of the reasons, regulatory divergence and fragmentation can increase the cost to UK firms seeking to sell products and services abroad. This is why it is important that the secondary objective includes consideration of international alignment, where possible.

More broadly, we would like to see the regulator giving careful consideration as to whether the secondary objective can be advanced by the UK regulators adopting outcomes-focussed standards and rules, as opposed to prescriptive requirements, without compromising standards in relation to the primary objectives.

3. What are some of the barriers in the current regulatory framework (including the role and responsibilities of other regulators and bodies such as the Payment Systems Regulator, The Pensions Regulator and the Financial Ombudsman Service) that could hinder efforts to drive economic growth and international competitiveness in (a) the UK economy and (b) the financial services sector?

Apart from the complexity of UK financial regulation and the burden it puts on firms in terms of compliance and other resource demands, we would point to the myriad of bodies which oversee it and their overlapping remits.

To take pensions as an example, the Pensions Regulator oversees corporate Defined Benefit schemes and Local Government Pension Schemes (around £1.9 trillion in assets), and the trust side of Defined Contributions (about £250bn+). The FCA regulates the contract side of Defined Contributions (roughly £350bn) as well as individual pensions (perhaps another £550bn+). In addition, the PRA supervises insurance companies providing bulk annuities (over £350bn and rising) which provide pensions for nearly two million people.

At a government level, the ‘P in DWP’ (pensions) sits in the Department for Work and Pensions, overlapping with HM Treasury, and HMRC. Each body produces their own data in a different way. To make matters worse, much of the official data on pensions gathered by the ONS is incomplete (by nearly £1 trillion) because it excludes individual pensions and

workplace contract pensions, as is most data on the number of pension pots and the number of individuals saving for a pension.

Consolidating these regulatory and government functions would potentially reduce costs, concentrate expertise, significantly improve pensions policy, enable faster and more effective reform, and hugely improve the quality and consistency of data in such an important area.[5]

4. Do the regulators have the right capability and capacity to fulfil their regulatory objectives on growth and competitiveness? To what extent might the culture of the FCA and PRA influence their ability to fulfil their growth and competitiveness objectives?

Regulators and firms share the challenge of keeping pace with technological change –and of the risks and opportunities these changes provide. It is imperative regulators continue to reflect on whether they have the expertise and resources they need now and will require in the future to fulfil their respective remits. While this will help to inform workforce planning and staff development, we would like to see greater use of secondments from the industry, enlarged budgets, increased salaries, and more training to attract and retain talent from the private sector would help ensure a higher degree of technical expertise and independence.

And as stated above, we believe there is potential to embrace a cultural shift away from eliminating risk and failure: this will require a degree of agility and a shift in culture at regulators, who should be granted occasional 'permission to fail'. This cultural shift could achieve much without significant weakening of regulatory standards in areas of consumer protection and market integrity.[6]

5. How effectively have the FCA and PRA consulted or engaged with industry in relation to the new secondary growth and competitiveness objective?

In our experience the FCA and the PRA are both highly collaborative in seeking a broad range of views through a combination of discussion papers (to capture early thinking), consultations (to capture FCA proposed rule changes), and policy statements (to set the scene on new rules to be introduced). There has also been numerous occasions in the past three years where the FCA and HMT have proactively sought abrdn's views on particular policy matters, which we find both efficient and encouraging.

[5] UK CAPITAL MARKETS: A NEW SENSE OF URGENCY, New Financial, co-sponsored by abrdn and Citi (September 2023)

[6] adapted from UK CAPITAL MARKETS: A NEW SENSE OF URGENCY, New Financial, co-sponsored by abrdn and Citi (September 2023)

There have also been instances where the pace of FCA consultation and industry engagement has been particularly efficient. However, in our experience this has typically been where there is an identified need to operate at pace such as when the FCA very effectively engaged with industry participants in consulting on rules to introduce side pockets for assets impacted by the Russia/Ukraine war in 2022.

That said, we also have seen examples of the sector being impacted negatively by the de-prioritisation of regulatory reform or where policy has been publicly proposed with insufficient engagement:

- In 2020 the FCA consulted on introducing notice periods for less liquid daily-dealing funds (CP20/15). We raised concerns that the majority of investors in our daily dealing Real Estate PAIF fund had voiced their intention to divest should the FCA clarify this view. The FCA's revised consultation has been repeatedly postponed from 2021, and now looks set to land in Q2 2025. In the meantime, we have seen 60% of investors exit this fund and a number of peer funds either close or reshape. Given the unique attributes of this asset class in giving retail investors direct exposure to Real Estate, it is disappointing to see end-investors making such decisions due to not knowing the FCA's future intentions. This led to abrdn's decision to convert its PAIF fund to a hybrid direct/indirect strategy ahead of the FCA's consultation paper.
- The Sustainable Disclosure Requirements (SDR) will apply to UK-based funds from December 2024, but the FCA has yet to consult on how SDR will apply to overseas funds being sold into the UK. This will mean that for example a retail investor looking at UK and Luxembourg-based funds on a platform might become more confused at how two otherwise identical funds are being displayed and described so differently.
- The FCA's recent proposals on publicising enforcement investigations (CP24/2) are an example of where policy has been developed with insufficient industry input on their potential impact. While the regulator has since sought to clarify that the proposed publication powers will be used infrequently, it is clear the very public announcement and debate which followed may have negatively impacted global views of the UK as a place to do business.

We would therefore encourage government and regulators to consider the potential impact of slow policymaking and the uncertainty associated with a lengthy regulatory process, and on the importance of consulting the industry at an early stage and taking account of its views.

The contra points to slow policy making are the FCA's recent approach to implementing swift change without alignment across industry sectors and conflicting regulatory obligations. For example, the application of regulatory forbearance for the disclosure of costs and charges for investment trusts[7], how this applies along the distribution chain and the contradictory requirement to comply with Consumer Duty.

The cadence of regulatory change is key to achieving the right outcomes for consumers and the industry.

6. In delivering their secondary objective on growth and competitiveness, what opportunities are there for the regulators to help to promote and support innovation in the financial services sector? How effective has the FCA's regulatory sandbox been for supporting greater innovation in the financial services industry?

Through the Smarter Regulatory Framework the FCA is already looking at ways in which assimilated law (legislation inherited from the EU) can be adjusted to better meet the needs of UK firms and consumers. We recognise that this is a large task, but ultimately the transfer of many rules from legislation into the FCA Handbook should help to make the UK regulatory environment more responsive and agile in the face of innovation and change. As a global investment company with experience of multiple jurisdictions we see it as essential that the regulatory regime is adaptable to the challenges of the 21st century – including the opportunities (and risks) created by digitalisation and Artificial Intelligence.[8]

Whilst abrdn entities have not yet participated in FCA regulatory sandbox activity we are supportive of the principle that firms can seek permission to pursue innovations in a proportionately supervised environment. We would encourage the FCA to continue to engage with firms and industry bodies on specific themes of technological change, as it has done on fund tokenisation and the work of the Technology Working Group of the Asset Management Taskforce. Regulatory involvement at an early stage is key to identifying and removing potential barriers to innovation, thereby allowing for the deployment of new technologies to be executed efficiently and in a controlled manner.[9]

7. How should the regulators ensure that any measures introduced to meet the secondary growth and competitiveness

[7] Statement on forbearance in relation to investment trust disclosure requirements | FCA
[8] abrdn response to Labour's 'Financing Growth' review (December 2023)
[9] UK Fund Tokenisation - A Blueprint for Implementation.pdf (theia.org); Further Fund Tokenisation - Achieving IF3 Through Collaboration Mar24.pdf (theia.org)

objectives work for businesses of all sizes across the sector, including startups, scaleups, and incumbents?

When considering new regulation or other regulatory developments the FCA should continue to perform cost benefit analysis on the basis of firm size, as well as making a strong case for any new regulation. The FCA should also recognise that regulatory change – even if it is positive change – can, when taken as a whole, have a compounding effect on the cost of implementation over and above the expected impact of any one measure.

It is reasonable that the FCA may focus supervisory activity on larger firms – who pose greater risks and are generally better resourced - than smaller firms. While the FCA is not expected to apply consideration of the secondary objective to decisions in respect of supervision, many elements of the FCA's existing rules are applied proportionately based upon firm size and activity. We support this risk-based approach to regulating firms. We would expect the regulator to continue to assess whether new measures introduced have disproportionate impacts on certain types of firm. We are encouraged that recent FCA communications on Consumer Duty have emphasised this proportionality. More widely the FCA fee structure is designed to ensure that firms bear the cost of regulatory activity based on their size and activities, with a "polluter pays" approach. This looks to ensure that "good" firms are not overly penalised by having to bear the costs associated with "bad" firms, an approach we support.

In respect of the 'polluter pays' principle, we recognise that part of the reason for a lower capital requirement for smaller firms is in the interests of proportionality and competition and enabling access to regulated financial advice. However, our view is that consumer protection should rank above those considerations and that, instead, access should be restricted to good quality, prudently managed regulated financial providers. In short, there is no longer room in the industry for firms which do not have sufficiently robust governance or capital reserves relative to the potential harms they can cause.

8. Are there any additional metrics over and above those already agreed by the regulators that would better enable stakeholders to track progress and support scrutiny of their work against the secondary growth and competitiveness objective? How should a measure of growth be included in these metrics?

We recognise the value of existing metrics in tracking the activity of the regulators and ensuring that they are accountable to stakeholders. However, as noted above, we are also aware of the inherent difficulties in capturing the precise economic impact of specific regulatory interventions.

It is understandably difficult to use traditional measures of economic growth to judge the performance of regulators against the secondary objective. Most economic levers are not held by regulators, and for the financial sector the most quantifiable metrics – volume of exports, people employed, total activity – are also subject to factors outside of the control of regulatory bodies.

We would highlight the work done by TheCityUK on how the UK might develop a framework to enable a proper international comparison of the activities and impact of UK regulators against their peers. This included developing comparative metrics capable of measuring, if indirectly, the impact of regulation on the ease of doing business for firms, for example monitoring time taken to implement changes to an authorised fund.[10]

9. Does the requirement within the secondary growth and competitiveness objectives to align with international standards create any constraints to fulfilling those objectives?

The FCA has defined international competitiveness in the context of its secondary objective as the attractiveness of the UK as a place to do business. Alignment between jurisdictions clearly contributes to making the UK an attractive place to do business for global firms. Firms operating across borders can encounter different obligations and compliance requirements for what is essentially the same product or service. In an ideal world all jurisdictions would align to recognised global standards. The next best option is to create regulatory frameworks which facilitate equivalence. Exports are a key driver of economic growth – and financial services accounted for £75.7 billion of UK exports in the 12 months to June 2024.[11] The FCA should be wary of pursuing changes which risk damaging the ability of UK firms to sell their products and services abroad. The FCA is an active participant at IOSCO level and has a key role to play in ensuring UK interests are represented in international policy discussions.[12]

10. Are the existing accountability measures around the secondary growth and competitiveness objective adequate?

Applying accountability and scrutiny to regulators is rightly a role for Parliament. However, for this scrutiny and accountability to be most effective, Parliament needs access to well-informed analysis of regulators' performance.[13] This relates to the development of appropriate metrics to measure the impact of regulatory activity – see answer to Q8.

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[10] advancing-international-competitiveness-and-economic-growth-how-do-financial-regulators-compare.pdf (thecityuk.com)
[11] UK trade in numbers (web version) - GOV.UK (www.gov.uk)
[12] Adapted from Budget Submission from the Investment Association Investing for Long Term Growth (October 2024)

11. Are there examples of regulatory policies in other jurisdictions that should be considered by UK regulators to help facilitate the new secondary objective? What might the FCA and PRA be able to learn and apply from comparable supervisors in other markets in terms of applying secondary objectives on growth and competitiveness?

We are aware that TheCityUK has done work on other jurisdictions where regulators have an existing growth or competitiveness aim or objective. It was generally positive on the approach adopted by the UK in terms of attempting to measure and assess the effectiveness of policy in achieving the secondary objective.[14] There is no silver bullet in terms of delivering growth and competitiveness, it is the cumulation of policy across a number of interlinked areas. For example, in the pension space our work with Citi has looked at international examples in an attempt to identify ways of unlocking the potential for investment in the UK pensions market - but you cannot simply copy and paste the system from one country to another.[15] UK policy needs to strike a careful balance between unlocking the potential of UK capital markets to promote investment in the UK, and on maintaining sufficient alignment with other jurisdictions to allow UK firms to easily do business globally.

1 November 2024

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[13] Adapted from advancing-international-competitiveness-and-economic-growth-how-do-financial-regulators-compare.pdf (thecityuk.com)

[14] Advancing international competitiveness and economic growth: how do financial regulators compare? | TheCityUK

[15] UK CAPITAL MARKETS: A NEW SENSE OF URGENCY, New Financial, co-sponsored by abrdn and Citi (September 2023)