

Alternative Investment Management Association (AIMA) – Written evidence (SCG0015)

The Alternative Investment Management Association (“AIMA”)¹ welcomes the opportunity to provide evidence to the House of Lords Financial Services Regulation Committee (the “Committee”) inquiry looking into the secondary international competitiveness and growth objective given to the Financial Conduct Authority (“FCA”) and the Prudential Regulation Authority (“PRA”) under the Financial Services and Markets Act 2023. AIMA members in the United Kingdom (“UK”) are primarily authorised and supervised by the FCA, so our response confines its comments to the FCA’s performance.

Robust, well-regulated capital markets benefit the wider economy. Academic research sponsored by AIMA shows that having a large capital market relative to the banking sector provides complimentary sources of funding and enhances economic growth.²

We are pleased to acknowledge that the FCA has been active in implementing the objective. For example:

- The creation of the Cost-Benefit Analysis (“CBA”) Panel³ is an important step forward in giving further rigour to this key part of the FCA’s rule-making process. It will give all stakeholders greater confidence as there will be more oversight to ensure that all the data relevant to a particular issue has been gathered and analysed and that the secondary objective has been taken fully into account. However, we believe more can be done to enhance the effectiveness of cost-benefit analyses, which we discuss below.

¹ The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with around 2,100 corporate members in over 60 countries. AIMA’s fund manager members collectively manage just over US\$4 trillion in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 250 members that manage over US\$2 trillion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors). For further information, please visit AIMA’s website: www.aima.org.

² See, Christoph Kaserer and Marc Steffen Rapp, Research Report, “[Capital Markets and Economic Growth: Long-Term Trends and Policy Challenges](#)” (March 2014).

³ *Details* of the CBA Panel are at, <https://www.fca.org.uk/panels/cost-benefit-analysis-panel>.

- The proposal to allow payment optionality for investment research will remove an unnecessary hurdle for asset managers which is out of line with non-European Union (“EU”) jurisdictions with significant asset management industries.⁴ It will make it easier for them to do business in the United States (“USA”) and also facilitate wider access to research material.
- The Overseas Funds Regime (“OFR”) is now active and provides a strong signal that the UK is open for business by allowing certain non-UK funds to be marketed to UK retail investors.
- The Long Term Asset Fund (“LTAF”) puts in place a new investment structure that can be used by all types of investors with long-term investment horizons in order to get access to a broader range of assets than are offered by most UK authorised funds.⁵
- A long-standing innovation pioneered by the FCA, the Regulatory Sandbox is a powerful demonstration of its commitment to fostering the growth of new technologies and businesses in a proportionate and risk-sensitive way.⁶

We would also like to take the opportunity to note the open and positive way in which the FCA communicates with the firms it supervises. This clear expression by the FCA of its expectations to firms on issues it sees as creating potential risks stands out internationally.

The FCA cannot be expected to ensure the competitiveness and growth of the UK financial services industry on its own. It is dependent on government more widely. For example, the FCA cannot begin its work on reforming the UK asset management regime until His Majesty’s Treasury (“HMT”) has completed its work and decided which UK Alternative Investment Fund Manager Regulations 2013 (“UK AIFMR”) powers to retain and which to devolve to the FCA.⁷

Just as important in taking affirmative steps to facilitate competitiveness and growth is the need not to undermine the UK’s position unnecessarily.

The continuing narrative from central banks that non-bank financial intermediation (“NBFII”) in general and investment funds in particular pose high risks to the financial system is misleading and risks undermining confidence in this vital UK sector. Continual emotive

⁴ See FCA, Policy Statement PS24/9, [“Payment Optionality for Investment Research”](#) (July 2024).

⁵ See FCA, Policy Statement PS23/7, [“Broadening retail and pensions access to the long-term asset fund”](#) (June 2023).

⁶ See the description of the FCA’s Regulatory Sandbox available at <https://www.fca.org.uk/firms/innovation/regulatory-sandbox>.

⁷ See the UK AIFM Regulations at, <https://www.legislation.gov.uk/ukxi/2013/1773/contents/made>.

references to well-established and highly-regulated and reported practices such as leverage as “hidden” or “excessive” is unjustified and damaging. Analysis should be based on clear evidence rather than what are often anecdotal concerns. We welcome the Bank of England System-wide Exploratory Scenario (“SWES”) stress test exercise of the UK financial system as a positive example of evidence-based analysis.

The FCA’s proposals to boost the frequency of disclosing that it has started enforcement investigations against firms is a clear example of an unnecessary proposal that will actively undermine the UK’s attractiveness as a leading international asset management hub. We sent a separate response to the Committee’s FCA enforcement guidance consultation inquiry on 11 October.

Annex 1

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

Completing the unfinished work of the Edinburgh Reforms will aid the FCA in achieving its secondary objective.⁸ Launched in 2022, the Edinburgh Reforms are designed drive growth and competitiveness in the UK’s financial sector. There are two areas in particular where work has begun and should be completed: securitisation and short-selling. We warmly welcome HMT’s recent decision to lay the Short Selling Regulation 2024 before parliament which will allow the FCA to begin work on amending its rules.⁹

Securitisation

Securitisation of assets helps boost economic activity by freeing space on firms’ balances sheets to make further investment. The current legislation on securitisation acts as a barrier to greater use of this beneficial financial technique. While AIMA fully agrees that securitisation may carry risks that need to be properly managed, the current rules prevent firms from maximising its benefits.

We believe that some targeted interventions and amendments could revive the UK securitisation market without introducing or increasing financial risk. This can be done by broadening the UK investors base for

⁸ A summary of the suggested reforms is available at: <https://www.gov.uk/government/collections/financial-services-the-edinburgh-reforms>.

⁹ See the Statutory Instrument and explanatory memorandum at [The Short Selling Regulations 2024](#) and [The Short Selling Regulations 2024 - Draft Explanatory Memorandum](#).

it, as well as allowing a wide range of financial institutions to engage in it and amending some details of the current rules on scope.¹⁰

Reporting

There is significant duplication in the data firms report, for example, in relation to some transaction reporting required under the UK MiFID framework.¹¹ Some reporting requirements, such as the asset stripping requirements in the UK AIFMR, should also be removed as Company Law already addresses the same issues.

There is also an opportunity to revisit the way in which risk is measured and reported to better assess it. Doing this would give a clearer picture of the amounts of leverage used by open-ended funds. It would also better align the UK with the International Organization of Securities Commissions (IOSCO) global recommendations and create better alignment with the USA and other international partners.

We set out our proposals in more detail in our response to the FCA's Discussion Paper DP23/2, *Updating and improving the UK regime for asset management*.¹²

As well as completing the Edinburgh Reforms, there are other changes the FCA can consider to further support the secondary objective.

Depositaries

The requirement for managers of professional funds primarily to use credit institutions to conduct custody and depositary services originated with AIFMD, transposed in the FCA Handbook in FUND 3.11, Depositaries.¹³ Prior to that it was common for managers of such funds to use prime brokers to carry out those services. This focus has led to a concentration of a small number of large UK depositary banks which are under constant pressure to push down on margins. This concentration also creates a potential threat to market stability in the event of the failure of one large player.

Depositary service providers to managers of professional-only funds are not subject to the extra requirements with which depositaries for managers of funds marketed to retail investors must comply. Managers of

¹⁰ For further details, please see AIMA's 2024 position paper, "[Reviving the UK securitisation market](#)" (August 2024).

¹¹ See the UK MiFID framework at, <https://www.fca.org.uk/markets/regulation-markets-financial-instruments>.

¹² For further details of DP23/2 see, <https://www.fca.org.uk/publications/discussion-papers/dp23-2-updating-and-improving-uk-regime-asset-management> and AIMA's response at, <https://www.aima.org/article/aima-publishes-its-response-to-the-fca-s-review-of-the-uk-asset-management-regime.html> (public access to be added).

¹³ See Article 21 of the AIFMD at, <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32011L0061>.

professional-only funds should have the option of using either a depositary bank or a selection of prime brokers which are able to discharge the relevant duties. This would not remove any protections but instead transfer the core regulatory safeguards to prime brokers. It could also have the ancillary benefit of improving choice and therefore competition.

Tokenisation

We strongly support the FCA's participation in Project Guardian, led by the Monetary Authority of Singapore with the Japan Financial Services Agency and the Swiss Financial Market Supervisory Authority.¹⁴ Project Guardian is a collaborative initiative with the private sector to explore the uses of tokenisation and decentralised finance. We believe the availability of tokenised funds could potentially lead to lower costs, wider access to illiquid assets and quicker settlement. Jurisdictions such as Luxembourg, Germany and France are already allowing tokenisation.

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?

As we discuss in our response to question 8, FCA senior management objectives should be aligned with the secondary objective. Active leadership from the top of the FCA will embed the thought processes and checks and balances needed to achieve the desired outcomes.

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?

No comment.

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?

Its people are the key to the FCA's success. It must recruit and retain staff at all levels with the right experience in a range of areas. This

¹⁴ For further details, see <https://www.mas.gov.sg/schemes-and-initiatives/project-guardian>.

includes staff with experience of how various types of firms in the financial services industry operate in practice, and not simply an understanding based on the rulebook itself. We understand that this is challenging as the FCA does not have the resources to compete with private sector pay. However, the combination of the FCA's mutually agreed resignation scheme ("MARS") in 2020/21¹⁵ and its Transformation programme in 2022 which changed pay and conditions has led to higher than normal staff turnover and industrial action.

The FCA should consider the effect of any further changes to staff pay and conditions on its ability to retain existing staff and attract new recruits with relevant practical experience.

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

No comment.

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?

The FCA Regulatory Sandbox is a very good example of how the UK can lead global thinking on regulatory and supervisory issues and we support its continuation and expansion.

7. How should the regulators ensure that any measures introduced to meet the secondary growth and competitiveness objectives work for businesses of all sizes across the sector, including startups, scaleups, and incumbents?

We welcome the establishment of the CBA Panel, as noted in our cover letter, and urge greater use of the Practitioner Panels as methods of ensuring that the secondary objective is taken properly into account. We also believe that a clear demarcation between the needs of wholesale and professional customers and the greater need for protection of retail customers will help the FCA to tailor its rules appropriately.

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

¹⁵ In 2021 MARS cost the FCA £7 million as 96 employees took up the offer. In 2022 it cost £800,000 as 10 employees took advantage of it. This has meant that FCA Group turnover in 2021 was 17.3% instead of 13.6% when the effect of MARS is taken out. See page 92, <https://www.fca.org.uk/publication/annual-reports/2021-22.pdf>

secondary growth and competitiveness objective? How should a measure of growth be included in these metrics?

We agree that it is important to be able to assess how successfully the secondary objective has been implemented, but at the same time we also recognise that it is challenging to do so. AIMA has previously provided HM Treasury with proposals on how this could be done.¹⁶

Capital market studies. The FCA should publish regular studies of UK capital markets to compare their functioning and effectiveness with other jurisdictions. This would provide clear empirical data on where the UK's competitive vulnerabilities do and do not lie and would allow better targeting of interventions.

Senior management responsibility. A management plan to embed the secondary objective in all relevant FCA processes along with ongoing monitoring should be a key objective.

Distinguish between professional and retail activities. Issues affecting retail consumers or mass market products will be very different to those facing wholesale or professional activities. They will have very different relationships with wholesale or professional international markets and their relative competitiveness.

FCA Practitioner and Consumer Panels. The existing FCA statutory panels can also have a role to play in assessing the objective.¹⁷ This could, for example, be a standing item in their annual reports.

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

We do not believe that this needs to be the case. The FCA is fully engaged with a range of global standard-setting bodies, notably IOSCO and the Financial Stability Board (FSB), and so has the opportunity to influence international standards to ensure such conflicts do not arise.

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

The FCA's publication of its annual report into how it is meeting the objective is a key piece of transparency. We believe it is important that both Parliament and HMT scrutinise regularly how the FCA is meeting the objective.

¹⁶ See <https://www.aima.org/resource/aima-responds-to-hm-treasury-s-call-for-proposals-on-how-to-assess-whether-uk-regulators-are-meeting-their-new-secondary-objectives.html> (public access to be added).

¹⁷ For more details on the statutory panels see, <https://www.fca.org.uk/panels>.

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?

Related to any metrics will be an understanding of how comparable regulators globally approach this issue. As we have already discussed, while the FCA can make greater strides, it cannot do this in isolation. For example, the Monetary Authority of Singapore (“MAS”) in 2020 put in place a new funds framework, Variable Capital Companies, along with co-funding of some expenses.¹⁸ This is on top of MAS’ work to promote Singapore as a destination for financial services firms looking to establish themselves in the Asia-Pacific region.¹⁹ This is part of the Singaporean government’s wider industrial strategy which includes the promotion of infrastructure and training as well as favourable tax treatment and help in setting up costs.

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¹⁸ For more details, see <https://www.mas.gov.sg/news/media-releases/2020/mas-and-acra-launch-variable-capital-companies-framework>.

¹⁹ See, e.g., the discussion at <https://www.mas.gov.sg/development/asset-management>.