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Submitted by e-mail to: dp23-2@fca.org.uk

Dear Michael,

CFA UK response to the FCA's Discussion Paper 23/2 – 'Updating and improving the UK regime for asset management'

The CFA Society of the UK (CFA UK) and CFA Institute jointly welcome the opportunity to respond to the FCA's discussion paper (the "DP") which serves as a useful review of both some legacy issues concerning current regulation and future issues raised by the advance of technology and digitisation. We thank you for meeting with us to briefly discuss some of them.

In line with our organisations' purpose (see Appendix I), with this letter we aim to highlight relevant issues to promote a regulatory environment where investors' interests come first, markets function at their best and economies grow and in a way that builds a more sustainable future. The list of issues raised in the DP is wide-ranging and we do not feel sufficiently informed to address all of them, so we have chosen to provide some relevant thoughts to some of the issues below.

Simplification/standardisation of the asset management regulatory regime (Q1-4)

We agree with the notion that regulation should aim for simplicity and be streamlined where possible. We therefore support homogenisation of rulebooks where it makes sense, such as a move towards a single rulebook for investment funds. This would reduce interpretation risk and reduce confusion in the minds of investors.

For Retail Funds, we are in principle attracted to the concept outlined in the DP of converting NURS to 'UCITS plus', though we have concerns that the underlying definitions of 'High New Worth' and 'Sophisticated' investors need updating. Benefits need to outweigh costs and any moves in this direction will need thorough consultation and cost benefit analysis. We share the concerns that changes such as this could take a long time to implement and contain unintended consequences. We also agree that UCITS is an internationally recognised and trusted framework and for this reason are less keen on the 'Basic Funds' concept which seems only to add to potential investor confusion by creating a third regime.

For Professional Funds, an increase in the small AIFM threshold (option 1) seems the least controversial and costly reform. Removing the threshold completely and basing it on some other criteria (option 2 in the DP) seems prone to abuse/circumvention - the riskiness of a fund is not just the type of strategy it follows but a whole host of factors - leverage, redemption rights, liquidity, concentrations etc. Prescribing all of this would get unwieldy and confusing and still could be open to abuse potentially if not drafted properly.

Improving the regulatory regime (Q5-13)

We support the opportunity of clarifying rules and expectations as regards outsourcing risks in general, and those which, in particular, relate to arrangements between authorised fund managers (AFMs) and delegated portfolio managers. The host AFM business model is vitally supportive of small firms, however, the quality of some host AFM Value for Money reporting and aspects of the Woodford scandal have clearly shown that this area of regulation could be tightened up. We believe the FCA could achieve this through typical thematic reviews by the FCA and the provision of subsequent guidance.

We also support the FCA's proposal to bring the ESMA guidance on fund stress testing into UK FCA Handbook. Aligning rules and practices in this domain will only serve regulators and firms in establishing sound risk management practices for the benefit of financial stability.

The issue of swing pricing has recently been consulted on by the SEC and CFA Institute Systemic Risk Council[1] provided three recommendations to improve the SEC's rule book. We also believe current regulation in the UK would benefit from a clarification of rules and expectations on dilution adjustments (swing pricing) to reduce risk of investor harm or reduce risk of firms interpreting principles in unintended manners.

We do not support excessive prescription of what investment due diligence should be, though we do believe the FCA could consider publishing guidance and best practice examples. Funds have different investment styles and approaches and this dictates different due diligence practices. Passive funds, in particular, do not utilise due diligence in the same way as active managers. Due diligence by credit funds, equity funds and sustainable funds will have common but also different areas of focus. For sustainable investment, as it is a new and fast evolving area, we would support the FCA either publishing a due diligence checklist or perhaps giving recognition to third-party due diligence checklists. Ultimately, however, we consider due diligence as a universal duty of investment managers to their clients; it is related to their ethics and professionalism and the application of their fiduciary duty. As the FCA has concerns, we think the FCA should approach this through thematic reviews to ascertain and confirm the credentials and professionalism of UK firms.

We do not, at this stage, support material changes to fund rules, either on eligible assets or on risk spreading. Such changes could introduce significant variations with the UCITS framework, without compelling evidence that reform is necessary. Again, we believe the FCA should conduct further analysis or market study, or perhaps a thematic review, before changing any of the existing rules. As suggested in 4.30, guidance on how the FCA believes the 10% rule should operate in different circumstances could be helpful and head-off a repeat of some of the practices that came to light in the collapse of Woodford.

[1] CFA Institute letter to the SEC (Feb 2023): https://www.systemicriskcouncil.org/2023/03/letter-of-the-systemic-risk-council-to-the-sec-on-rules-for-open-end-funds/

Technology and innovation (Q14-18)

For technology and innovation, our view is that the FCA should continue to apply the principle of 'same risk, therefore same regulatory outcome'. In other words, new regulation is only required if a new technology raises concerns that it might threaten or undermine the objectives and outcomes of existing regulation. We would not support new regulations for new products just because they are 'new' and if they are not necessary.

Innovating investor engagement through technology (Q18-22)

As expressed in our response to the joint response letter formulated by CFA Institute and CFA UK on the Future Disclosure Framework (DP22/6)[2], we favour making use of new technological capacity to allow modularity in reporting and disclosures, so as to facilitate investor engagement and permit information to better reflect investors' needs or concerns. Our letter also calls for a revision of the division of responsibilities between the manufacturer and the distributor in the investment chain. We believe the prospectus can be improved and modernised and are supportive of the suggestions in the DP.

We greatly appreciate the opportunity to respond to this consultation and would welcome continuing our ongoing dialogue on this broad range of topics raised in the DP.

Yours sincerely,

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CFA Society of the UK

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Head of Advocacy and Policy Research, EMEA
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With thanks for the oversight of the Professionalism Steering Committee.

[2] CFA UK and CFA Institute joint response to the FCA on DP22/6 (March 2023): https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/3-research-and-position-papers/cfai_cfauk_response_fca_fdf_final-post-psc.pdf

APPENDIX I: About CFA UK and CFA Institute

CFA UK serves nearly twelve thousand leading members of the UK investment profession. Many of our members work either managing investment portfolios, advising on investments, or in roles responsible for investment operations or oversight.

The mission of CFA UK is to build a better investment profession and to do this through the promotion of the highest standards of ethics, education and professional excellence in order to serve society's best interests.

Founded in 1955, CFA UK is one of the largest member societies of CFA Institute and provides continuing education, advocacy, information and career support on behalf of its members.

Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

For more information, visit www.cfauk.org or follow us on Twitter @cfauk and on LinkedIn.com/company/cfa-uk/.

CFA Institute is the global association for investment professionals that sets the standard for professional excellence and credentials.

The organisation is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow.

It awards the Chartered Financial Analyst® (CFA) and Certificate in Investment Performance Measurement® (CIPM) designations worldwide, publishes research, conducts professional development programs, and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.

CFA Institute has members in 162 markets, of which more than 170,000 hold the Chartered Financial Analyst® (CFA) designation. CFA Institute has nine offices worldwide and there are 158 local member societies.

For more information, visit www.cfainstitute.org.