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Investment Management Alert

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Financial Conduct Authority's Asset Management Review – Authorised Funds Shake Up

On 28 June 2017, the Financial Conduct Authority (FCA) published the Asset Management Market Study Final Report (the "Asset Management Review") as well as a Consultation Paper setting out some proposed changes to the FCA's rules, reflecting the FCA's findings in the Asset Management Review ("Consultation Paper").

The FCA had launched the market study into the UK asset management industry in 2015 in order to assess whether the market is operating efficiently and whether investment products offer value for money.

Who Does it Apply to?

The Asset Management Review focused on the UK investment managers and management companies (including The Undertakings for Collective Investment in Transferable Securities (UCITS) Management Companies) of authorised funds (AFMs). Most of the conclusions and all of the proposed changes in the Consultation Paper relate to UK AFMs[1]. The FCA did not include alternative asset classes as part of its analysis.

The proposals in the Consultation Paper will not apply to non-UK UCITS management companies or to UK or non-UK Alternative Investment Fund Managers that manage or market unregulated funds in the UK.

Does it Impact Non-EU Managers?

US and other non-EU investment managers are not affected by the findings in the Asset Management Review or the proposed rule changes in the Consultation Paper. Some of the elements, such as greater charges disclosure, however, may have an indirect impact on contractual negotiations with investors.

Does it Impact UK Managers of Unregulated Funds?

UK investment managers of unregulated funds and segregated accounts are generally unaffected by the Asset Management Review or the proposed rule changes in the Consultation Paper.

FCA Findings in the Asset Management Review

The FCA found that the market for authorised funds in the United Kingdom showed weak price competition in a number of areas which, in turn, has a material impact on investors' net investment

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[1] Specifically, UK-authorised firms that directly manage collective investment schemes which are authorised and domiciled in the United Kingdom, as well as UK UCITS management companies managing European Economic Area (EEA) UCITS schemes.

returns. The FCA also found that funds did not, on average, outperform their own benchmark after fees and that there was no evidence of positive correlation between higher fees and better performance. Consequently, the FCA is considering penalising managers who charge performance fees, but underperform their benchmarks, and only permitting managers to charge performance fees if the performance exceeds any previous high-water mark. In addition, the FCA will:

- consider introducing an all-in fee for retail investors that includes an estimate of trading costs and is likely to issue a separate paper on this later
- seek further information on whether to end the payment of trail fees on funds sold before 2012
- request that an independent person convene a group of industry and investor representatives to develop a template for standardised disclosure of costs and charges to institutional investors.

Proposals

The Consultation Paper sets out proposals which seek to implement some of the remedies identified in the Asset Management Review. In summary:

- Value for Money

  AFMs would have to assess, on an ongoing basis, whether value for money has been provided to fund investors. AFMs would be required to document and report on the findings of the assessment and any actions resulting from the same at least annually.

- New Senior Manager Prescribed Responsibility

  Introduction of a new specific Prescribed Responsibility under the Senior Managers and Certification Regime[2] (SMCR) to ensure that AFMs comply with the obligation to act in the best interests of investors (including assessing value for money). This will be subject to a separate consultation by the FCA.

- Independent Directors

  AFMs would be required to appoint independent directors to the board. A minimum of two directors and at least 25 per cent of the total board should be appointed. Such independent directors would be appointed for limited terms and could not be employees or recent former employees of the AFM or its group.

- Moving Investors into Better Value Share Classes

  AFMs will have powers to undertake a mandatory share class conversion to move investors into a better share class.

Next Steps

The FCA has asked to receive comments on its proposals by 28 September 2017.

The FCA has also indicated that there are further areas in which the FCA wants to do more work. The FCA has set out its current thinking on issues including fund objectives, use of benchmarks, performance

[2] To take effect with respect to asset managers in 2018.

reporting and the transparency of fees and charges in the AMMS Final Report, and it plans to consult on these further issues, where relevant, later on in the year.

Contact Information

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