

May 21, 2023

Asset Management and Funds Policy Team  
Wholesale Buy-side Division  
Financial Conduct Authority  
12 Endeavor Square  
London E20 1JN  
Submitted electronically to: [dp23-2@fca.org.uk](mailto:dp23-2@fca.org.uk)

**Re: Updating and improving the UK regime for asset management**

Dear Sir/Madam:

ICI Global<sup>1</sup> appreciates the opportunity to provide feedback to the Financial Conduct Authority (FCA) on its discussion paper seeking feedback on how the FCA can modernize the regime for funds and asset managers to improve outcomes for UK markets and consumers (Discussion Paper).<sup>2</sup> ICI's mission is to strengthen the foundation of the asset management industry for the ultimate benefit of the long-term individual investor. Our members invest on behalf of millions of retail investors around the world choosing funds to save for retirement, education, and other important financial goals. The Discussion Paper is, therefore, of great interest to our members, many of whom operate in the UK and offer funds and other investment products to retail investors.

We support the UK government's efforts to implement a regulatory framework that fosters innovation and the use of modern technology for the benefit of investors. We first provide below some general comments for the FCA's consideration, followed by responses to certain of the FCA's specific questions.

General Comments

The FCA states that it will seek to ensure that any changes that are made are effective and proportionate. As the FCA considers how to prioritize potential changes, we recommend that the FCA focus on issues or areas where revisions are necessary rather than make changes where the cost/benefit calculus is less clear. In addition, the FCA should avoid making changes that are unduly disruptive to either investors or asset managers unless there is a substantial benefit from such a change. Global fund managers have recently been, and are continuing to be, inundated with regulatory changes that require firms to devote significant financial and personnel resources to

---

<sup>1</sup> [ICI Global](#) carries out the international work of the [Investment Company Institute](#), the leading association representing regulated investment funds. With total assets of \$38 trillion, ICI's membership includes mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and UCITS and similar funds offered to investors in Europe, Asia and other jurisdictions. ICI's mission is to strengthen the foundation of the asset management industry for the ultimate benefit of the long-term individual investor. ICI Global has offices in Brussels, London, Hong Kong, and Washington, DC.

<sup>2</sup> The Discussion Paper is available at <https://www.fca.org.uk/publication/discussion/dp23-2.pdf>.

implement new regulations and ensure compliance. UK asset managers, specifically, have been grappling with the changes to the consumer duty, the senior manager certification regime, the sustainable disclosure regime, enhanced ESG reporting, the wholesale markets regulation, and a new retail disclosure framework, among others. Changes that are mere tinkering would add to this regulatory burden without commensurate benefit.

The FCA also states that it will seek to ensure that any changes are consistent with international standards, so that firms can continue to operate efficiently on a global basis. We agree that this is an important principle to adhere to in this process. We request that, where the FCA intends to deviate from international standards, particularly from the approach taken in EU regulations, the FCA carefully consider the costs to regulated funds and investors and explain the rationale behind such change. Asset managers often can serve their clients best when they are able to scale their products. For this to be possible in UK markets, it's important to maintain a rule set that is closely integrated with other major international jurisdictions like the United States and the European Union. The more that new UK rules diverge from the EU's rules, the greater the increase in costs and burdens to UK asset managers operating throughout Europe.

### Responses to Select Questions

#### Question 1

*Do you think that we should aim to create a common framework of rules for asset managers? What benefits would you see from this? What costs might this create? If you do not think we should do this, are there any areas discussed above where we should consider taking action, even if we do not create a common framework of rules? What would we need to consider around the timing of implementing a change like this?*

We understand the rationale for the FCA exploring whether it should create a common framework of rules. Asset managers operating in the UK (in particular those with global businesses) have already been subjected to a myriad of regulatory changes in recent years, and implementing those changes have often required substantial investment in time, budget, and resources. The creation of a common framework would impose significant costs and burdens on top of fully-stretched budgets and personnel that would outweigh the potential benefits of the framework. For these reasons, we recommend that the FCA not proceed with such an undertaking at this time.

#### Question 2

*Do you think we should change the boundary of the UK UCITS regime? If so, do you think we should take any of the three approaches set out there? Should we consider any alternative approaches? What timeframe would be needed to allow firms to change their existing product offering or to develop new products?*

There are significant benefits to retaining the UK UCITS brand. We suggest that the FCA not change the boundary between the UK UCITS and non-UCITS retail scheme (NURS) regimes for these reasons:

- It is much more efficient and less costly for asset managers already offering EU UCITS to establish retail funds in the UK under the familiar and well-known UCITS regulatory structure. This broadens the appeal of operating retail funds in the UK.

- The UCITS structure is well-understood and highly regarded by investors throughout the world. It will serve the UK well to maintain the UCITS brand, which is trusted in Asian and Latin America markets.
- Changes to the boundary between UK UCITS and NURS, or the creation of new categories of funds, such as “basic funds” or “UCITS plus” as proposed by the FCA, would, in our view, cause confusion as to the difference between a UK UCITS and an EU UCITS, and would make comparison between these products more difficult.
- Regulatory divergence resulting from changes in the boundaries between UK UCITS and NURS would increase distribution challenges under the Overseas Fund Regime and investor confusion.

#### Question 5

*Do you think that we should amend our fund rules or add guidance either to make clearer the requirements on portfolio managers of funds, or to set minimum contractual requirements between host AFM and portfolio managers? Do you think this would lead to any other consequences that we need to consider?*

We support the principle of requiring authorized fund managers (AFMs) to comply with certain minimum standards in order to ensure an appropriate degree of investor protection. We therefore believe that there would be benefit in having clarification on the requirements that apply to portfolio managers of funds to alleviate potential areas of confusion. Any such changes should result in provisions or requirements that are not unduly prescriptive, complex, or burdensome. We therefore urge the FCA to carefully strike an appropriate balance between clarity and flexibility.

#### Question 6

*Do you have any comment on us potentially amending the rules and guidance around liquidity stress testing?*

We support the FCA proposing and consulting on changes to the rules and guidance around liquidity stress testing. In particular, we support converting the liquidity stress testing guidelines issued by the European Securities and Markets Authority into rules and guidance in the FCA Handbook. We also support removing or restricting the qualification “where appropriate” in COLL 6/12/11R(2), which limits the stress testing requirement by providing fund managers with a reason not to carry out stress tests.

The liquidity management rules applicable to funds, however, should not be extended to separately managed accounts/portfolio management services. For separately managed accounts, liquidity management is best governed through the investment management agreement entered into between the parties, which is able to take into consideration a client’s particular circumstances, including the source of the funds.

### Question 7

*Do you have any comments on whether we should make our rules on liquidity management and anti-dilution clearer?*

We support the FCA reviewing the existing rules on dilution adjustments and other anti-dilution mechanisms and revising such rules to make clearer the FCA's expectations regarding their use. ICI has undertaken substantial research on dilution in US markets and found that the effects are largely non-existent for equity funds and minimal for bond funds. We urge the FCA to consult with relevant stakeholders regarding any proposed changes in order to ensure that the rules achieve FCA's goals and are practically workable for fund managers. We would be delighted to share ICI's research on dilution.

### Question 11

*Do you have comments on the analysis of the eligible assets rules for UCITS set out here? Do you think we should update or provide guidance on these rules? If we did so, what impact would this have for managers of UCITS funds?*

The FCA has expressed concern that some UCITS managers might perceive the 10% rule, which generally permits UCITS to invest up to 10% of their portfolio in assets that do not meet the eligible markets criteria, as permission to invest that part of the fund in a wider range of assets (that do not meet the eligible market criteria) without considering the implications for suitability or risk management. We support the FCA providing clarifying guidance on this matter. However, as the FCA considers providing any such guidance, we caution it to carefully consider the important and valuable function of the 10% bucket and to ensure that any such guidance does not unduly restrict its use in appropriate circumstances. For example, certain external events, such as the start of the Russia-Ukraine war and corporate actions, may warrant the use of the 10% bucket for the benefit of investors.

### Question 12

*Do you have any comments on whether we should consider removing or modifying detailed or prescriptive requirements in the rules on prudent spread of risk?*

We advise the FCA against changing the rules regarding the prudent spread of risk, such as the (5/10/40 rule). While we recognize that a more principles-based regime may provide for greater investment flexibility than the current regime based on quantitative requirements, the well-established 5/10/40 rule is one of the foundations of the UCITS regime on diversification and is one of the reasons the UCITS regime is globally trusted and respected. We believe that any benefit derived from changing this provision would be outweighed by the drawbacks.

### Question 13

*Are there any other areas where you think we should consider removing or modifying prescriptive requirements in the retail fund rules?*

We recommend that the FCA consider permitting UK UCITS to receive collateral by way of security interest (pledge) rather than only by transfer of title as is currently required under the FCA's rules. Securities lending is undertaken by UK UCITS as part of their efficient portfolio

management strategies, and generates incremental revenues from their asset holdings, thereby increasing returns for investors. Due to the legal requirement to receive collateral under a title transfer agreement, UK UCITS have been unable to use the alternative method of collateralization that has recently emerged whereby lenders take a security interest (rather than title to) the collateral. As a result, the lendable inventory of UK UCITS is underutilized and they are at a competitive disadvantage compared to lenders that are not subject to the same limitation. Because security interest collateral arrangements have been structured such that they are legally akin to title transfer arrangements, we believe that this change could be made without introducing incremental risk to UK UCITS and their investors.

#### Question 14

*Do respondents agree that we should work toward consulting on rules to implement the “Direct2Fund” model?*

We strongly support the FCA working towards consulting on rules to implement the “Direct2Fund” model. An optional model that would make it possible for investors to transact directly with the fund when buying and selling units, if implemented in a manner that appropriately addresses regulatory issues and concerns, could be beneficial to both fund managers and investors.

#### Question 15

*What benefits would tokenized units in authorized funds provide for investors? What regulatory changes would be needed to enable tokenized units to be issued? How much of a priority should be put on enabling tokenization of units?*

Tokenized units in authorized funds may provide benefits to investors, but, before allowing tokenized units to be issued, the FCA should ensure that it has fully considered and tested all aspects of tokenization. We suggest that, if the FCA proceeds with this, it consider operating a “sandbox” so that any issues that may arise can be ironed out in a more controlled environment.

#### Question 19

*Do you agree that improving the content and readability of the prospectus will improve investor engagement? What specific changes would you like to see?*

We believe that improving the content and readability of the prospectus has the potential to improve investor engagement. However, because of the resource outlay and IT costs that would likely accompany the implementation of any such changes, we urge the FCA to consult with industry and investor groups to gain a fuller understanding of what changes would most effectively improve investor engagement.

As expressed in our response to the FCA’s discussion paper DP22/6, which set out the FCA’s thinking on the future disclosure framework for retail investors, we recommend that the FCA permit the use of digital disclosure as the default for disclosures and information and allow information in investor disclosures to be delivered in either document form (e.g., as a PDF) or non-

document form (e.g., on a mobile phone or webpage).<sup>3</sup> We also recommend a disclosure approach that permits the layering of information, for example with the first layer containing general/key information and the second layer containing descriptive/additional information and links to external sources. In our view, a less prescriptive disclosure regime that fosters the use of digital disclosure will facilitate more innovative disclosure to the benefit of retail investors.

#### Question 20

*What changes to the rules for managers' reports and accounts could enable firms to make best use of technology to meet investors' information needs? How else could disclosure of ongoing information to fund investors be improved? For example would there be benefit in us consolidating ongoing annual disclosure reports for funds?*

Detailed portfolio holdings are contained in annual and half-yearly reports. The FCA states that they could consider requiring portfolio holdings to be published more frequently – quarterly, or even monthly – because this may be useful for investors when there are significant portfolio changes or adjustments to investment strategy. As the FCA considers this issue, we recommend that the FCA not introduce portfolio holdings disclosure requirements that would require disclosure at a higher frequency (e.g., monthly) than is currently required in other key jurisdictions such as the United States and European Union. Frequent disclosure of full portfolio holdings by active fund managers brings an increased risk of copycatting, which is particularly concerning for portfolio managers that utilize investment strategies across their global range of products. Further, the FCA's suggestion that reports and accounts can be published more quickly and easily in a digital world fails to take into account that most of the production time is driven by the time needed to prepare and audit those reports and accounts. This is not something that can be done easily and quickly with the necessary diligence and accuracy; therefore, a time lag will always be necessary.

#### Question 24

*Do you have any comments on potential reform of the UK regulatory regime for asset managers and funds in areas that are in scope of this paper but have not been discussed in detail?*

In its December 2022 consultation on PRIIPS and UK Retail Disclosure, HM Treasury stated that a key ambition is to continue improving choice of investment products for retail investors, including by taking measures to ensure that retail investors can access a wide-ranging set of investment products from different jurisdictions. We support this ambition and specifically recommend that, as part of these measures, the FCA take steps to make it easier for retail investors to access products such as exchange-traded funds domiciled in the United States.

\* \* \* \* \*

---

<sup>3</sup> See ICI Global letter to Retail Investment & Distribution Policy, Financial Conduct Authority, dated March 7, 2023, available at <https://www.ici.org/system/files/2023-03/23-global-cl-fca-future-disclosure-frmwrk.pdf>

ICI Global and its members appreciate the opportunity to provide feedback on this issue. If you have any questions regarding our response, please contact Michael N. Pedroni at +1-202-876-5352 or michael.pedroni@ici.org or Eva Mykolenko at +1-202-657-7926 or emykolenko@ici.org.

Sincerely,

/s/ Michael N. Pedroni

Michael N. Pedroni  
Chief of ICI Global