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Dear FCA,

Financial Services Consumer Panel response to CP26/28 The UK AIFM Regime

The Financial Services Consumer Panel welcomes the opportunity to respond to the FCA's Consultation Paper CP26/28 *The UK AIFM Regime*. The Panel supports the FCA's objective of creating a simpler, more proportionate and more coherent regulatory framework for alternative investment fund managers. However, simplification should not come at the expense of consumer protection, market integrity or regulatory accountability.

In considering these proposals, the Panel urges the FCA to retain a clear consumer-protection lens. Consistent with our earlier response to the FCA's Call for Input on the future regulation of alternative investment fund managers, we believe that all firms should continue to be subject to high minimum standards, including the Consumer Duty, effective governance and senior management accountability. Regulatory categorisation and prudential requirements should reflect the full range of risks that may lead to investor harm, rather than relying primarily on firm size or leverage.

The Panel's overarching view is that regulatory reform should continue to be driven by consumer outcomes rather than by firm size alone. While proportionality is an appropriate objective, the regulatory framework should remain risk-based and ensure that firms managing activities capable of causing significant consumer harm are subject to appropriate governance, prudential and conduct standards regardless of their size.

The Panel supports retaining core safeguards within the AIFM regime while reducing unnecessary complexity. In particular, simplification of the prime broker and wider operating conditions should preserve protections relating to custody, asset segregation, conflicts of interest, transparency and accountability. Where retail consumers have direct or indirect exposure to alternative assets, firms should continue to receive complete, clear, understandable and timely information about material risks. Firms should test consumer-facing communications with their

target market, and consumers should continue to benefit from appropriate complaints, compensation and redress arrangements. Simplification should not result in weaker protections, reduced accountability or inconsistent standards between comparable products and services.

The Panel welcomes the FCA's review of the prudential framework for fund managers and supports a proportionate model combining minimum baseline requirements with additional risk-sensitive measures. Prudential requirements should reflect not only firm size, but also the nature of activities undertaken, liquidity characteristics, leverage, valuation complexity, outsourcing arrangements and the potential for consumer harm. Firms should hold sufficient financial and operational resources to prevent consumer detriment, support orderly wind-downs and provide timely redress where necessary.

The Panel also supports improvements to supervisory reporting and data collection where these enhance the FCA's ability to identify emerging risks while avoiding unnecessary duplication for firms. Reporting should focus on indicators of consumer harm, operational resilience, governance failures and emerging risks that allow supervisory intervention before harm becomes widespread.

More broadly, the Panel encourages the FCA to use the reforms to improve consistency across the wider asset management regime. Consumers facing comparable investment risks should receive comparable standards of protection irrespective of the legal structure through which they invest. Simplification should therefore strengthen regulatory coherence while maintaining high standards of governance, transparency and accountability across the sector.

Overall, the Panel considers that the proposed reforms provide an opportunity to modernise the UK AIFM regime, provided they continue to place consumer protection at the centre of regulatory design and ensure that proportionality is balanced with effective safeguards for investors and financial stability.

Yours sincerely,

Chris Pond
Chair, Financial Services Consumer Panel

Annex A – Responses to CP26/28 The UK AIFM Regime

35. Do you agree with our intention to broadly retain but simplify the existing requirements for prime brokers, subject to any changes we make to the depositary regime? Is there anything else relevant that we should consider?

We broadly agree with retaining the existing requirements for prime brokers while simplifying them, provided that simplification does not weaken consumer protection or reduce safeguards around custody, asset segregation, conflicts of interest, reuse of assets and oversight of leverage.

Although many AIFs are not mass-market retail products, retail consumers can still be affected directly where they invest through long-term asset funds, pension arrangements, investment platforms, advised portfolios or other structures with exposure to alternative assets. A clearer and more proportionate regime may benefit consumers if it reduces unnecessary costs that are ultimately passed through to investors and makes responsibilities easier to supervise.

However, the FCA should ensure that any simplification does not reduce transparency for investors or weaken protections where prime brokerage arrangements create complex counterparty, collateral or rehypothecation risks.

Consistent with our earlier response, the FCA should not rely on self-certification alone where products or arrangements are available only to professional or accredited investors. Firms and distributors should hold documented evidence that the investor meets the relevant criteria before investment, particularly where prime brokerage or leverage arrangements may increase the complexity of the risks borne by investors.

The FCA could improve the proposal by requiring firms to explain, in consumer-facing language where retail investors may be exposed, the practical impact of prime broker arrangements on asset safety, liquidity and loss recovery in a stress event.

36. Do you agree with our approach to consequential changes in these sourcebooks? If not, what do you disagree with and what alternative approach would you suggest?

We support the FCA's approach to consequential changes where they are necessary to keep the Handbook coherent and avoid inconsistent requirements across sourcebooks.

From a consumer perspective, consequential changes should be judged not only by whether they reduce regulatory duplication for firms, but also by whether they preserve clear accountability, fair treatment and effective supervision. Where rules are removed, simplified or cross-referenced, consumers should not experience any reduction in protection or redress.

The FCA could improve the proposal by publishing a clear consumer-impact mapping of the main consequential changes, showing whether protections are retained, strengthened or removed. This would help stakeholders assess whether technical rule changes have any practical effect on retail consumers, particularly in areas such as disclosure, complaints, governance, valuation and liquidity management.

The Panel would also encourage the FCA to use consequential changes to close any gaps that have enabled firms to navigate around the perimeter or apply weaker standards to products that consumers would reasonably view as comparable. A simpler regime will only benefit consumers if it makes protections easier to understand and prevents arbitrage to the detriment of investors.

Any removal or simplification of requirements should be supported by a clear evidence base demonstrating that consumer protection and market integrity will not be adversely affected. Where protections are removed because they are considered disproportionate, the FCA should explain how equivalent consumer outcomes will continue to be achieved.

37. Are there areas of the asset management regime we should consider first to ensure consistency and remove unnecessary differences in our rules?

The FCA should prioritise areas where unnecessary differences between regimes could create consumer confusion or arbitrage between product types. These include disclosure standards, liquidity management, valuation, conflicts of interest, governance, delegation and wind-down expectations.

Retail consumers should receive comparable protections where they face comparable risks, regardless of whether the product is structured as an authorised fund, an alternative fund, a long-term asset fund or is accessed indirectly through another investment wrapper.

Consistency should not mean lowering standards to the least demanding regime. The FCA should use this reform to align rules around the consumer outcome they seek to deliver: clear information, suitable distribution, robust governance, value for money, operational resilience and effective redress where things go wrong.

We encourage the FCA to treat consistency as a means of achieving equivalent consumer outcomes. Where different regimes expose consumers to similar risks, protections such as clear disclosure, governance, complaints handling, access to the Financial Ombudsman Service and Financial Services Compensation Scheme coverage should be safeguarded unless there is a clearly evidenced reason for a different approach.

Where the FCA proposes to remove or simplify disclosure requirements on the basis that they are considered of limited value, it should support those decisions with

evidence, including consumer research where appropriate, to demonstrate that the information is genuinely not useful or that an alternative approach would deliver better consumer outcomes.

This is particularly important for listed closed-ended investment companies and other structures with material retail ownership. Where consumers are exposed to complex or illiquid assets, consistency should preserve access to redress and should not remove AIFM-related protections unless equivalent safeguards are demonstrably available elsewhere in the regulatory framework.

38. What are your views on the options we have presented? Are there other approaches that we should consider?

The Panel understands that the FCA is considering removing the current rule that restricts AIFMs largely to fund management activities. And that FCA is exploring different options for allowing firms to undertake a wider range of regulated activities, with any changes accompanied by a revised prudential framework.

The Panel believes that greater flexibility could make firms more efficient and encourage competition. However, allowing firms to undertake more activities may also increase operational complexity, conflicts of interest and the range of risks consumers are exposed to unless governance and prudential safeguards remain robust.

The Panel is overall supportive of the FCA's decision to review the prudential framework for fund managers and to consider whether the current requirements remain proportionate, coherent and effective.

The options presented should be assessed primarily by whether they ensure firms have sufficient financial resources, liquidity, insurance and wind-down capability to prevent or remedy harm to investors. Retail consumers may be affected directly where they invest in AIFs or authorised alternative funds, and indirectly through pensions, platforms, advised portfolios or other investment wrappers. For those consumers, the prudential regime matters because weak firm-level resources can lead to poor communications, delayed redress, disruption to fund operations, disorderly transfers or increased costs being passed on to investors.

We would favour an approach that combines a simple baseline requirement for all fund managers with risk-sensitive add-ons where the potential for investor harm is greater. A purely size-based framework may be easier to administer, but it could understate the risks of smaller firms managing complex, illiquid or highly leveraged funds. Conversely, a framework that is too complex could increase compliance costs which may ultimately be passed on to consumers. The FCA should therefore calibrate requirements by reference to the nature of the manager's activities, assets under management, fund liquidity, leverage, valuation complexity, outsourcing, retail or pension exposure, complaints and redress risk.

The FCA could improve the proposal by making consumer harm a specific calibration factor in any prudential model. In practice, this should mean requiring firms to hold resources that are sufficient not only to meet minimum capital formulae, but also to manage operational incidents, compensate investors for errors or misconduct, maintain critical services during stress and carry out an orderly wind-down. We would also encourage the FCA to consider clear reporting indicators for near-misses, operational errors, redress events and liquidity stress, as these would help supervisors identify consumer harm before it becomes widespread.

This approach should also recognise that risks to consumers may arise from firm culture, governance, product design, distribution, valuation, operational resilience and treatment of investors, as well as from balance sheet size or leverage. A risk-based prudential framework should therefore incentivise firms to maintain good business practices and to evidence how they prevent and remedy consumer harm.

39. Do base capital requirements, activity-based requirements and fixed overhead requirements appropriately reflect the scale and nature of fund managers' activities and, if you think they do, how should they be calibrated?

The Panel notes that the FCA is considering replacing the current AIFM prudential regime with a more proportionate framework based on three elements: minimum base capital, activity-based capital and fixed overhead requirements. It is now seeking views on how these should be calibrated for different firms

The Panel believes that adequate capital helps firms absorb losses, correct mistakes and continue operating during periods of stress. If capital requirements are too low, consumers may suffer greater disruption, delayed redress or higher costs if a firm encounters financial difficulties.

The Panel therefore notes that base capital, activity-based requirements and fixed overhead requirements should reflect both the scale of a manager's activities and the nature of the harm that may arise if the firm fails or acts improperly. For retail consumers, the key question is whether the manager has sufficient financial resources to operate responsibly, correct errors, support orderly wind-down and meet liabilities without transferring avoidable costs or disruption to investors.

The Panel also supports a calibrated framework that combines a minimum base level, a metric linked to activity and a fixed overhead component. Calibration should be sufficiently risk-sensitive to capture fund complexity, assets managed, use of leverage, liquidity mismatch, outsourcing, retail exposure and the potential need for redress. The FCA should avoid a framework that is too low to protect consumers or so blunt that firms managing higher-risk products benefit from lower requirements simply because their balance sheets are simple.

40. To what extent should the risk of compensating investors for errors, negligence or misconduct, which can scale with assets under management, inform the design of activity-based metrics for fund managers?

The Panel notes that FCA is exploring whether firms that manage larger or more complex funds should hold additional capital to reflect the potential costs of compensating investors for operational errors, negligence or misconduct. The Panel agrees that if firms hold sufficient resources to compensate investors when things go wrong, consumers are more likely to receive timely redress. If these risks are underestimated, firms may struggle to meet liabilities following operational failures or misconduct.

The FCA could improve the proposal by including metrics that reflect the probability and scale of consumer redress, including history of errors, volume of affected investors, complexity of valuation, reliance on third-party service providers, concentration of retail or pension exposure and the availability and limits of professional indemnity insurance. The framework should encourage firms to prevent harm rather than merely hold capital after risks have crystallised.

41. To what extent are firm-level liabilities and the costs of wind-down significant for fund managers, and should they be subject to a basic liquid asset requirement; if so, how should this requirement be calibrated?

Firm-level liabilities and wind-down costs are significant for consumers because the failure of a manager can create disruption, uncertainty, communication failures and practical barriers to accessing or transferring investments, even where fund assets are segregated. A basic liquid asset requirement would help ensure that firms can continue essential functions, communicate with investors, oversee service providers and execute an orderly transfer or closure without undermining consumer outcomes.

The Panel notes that the FCA is considering whether fund managers should hold a minimum amount of liquid assets (such as cash or assets that can quickly be converted into cash) to enable them to meet their obligations and fund an orderly wind-down if necessary. The Panel believes that adequate liquidity helps ensure firms can continue communicating with investors, transfer funds smoothly and manage an orderly closure without unnecessary disruption. Without sufficient liquidity, consumers could face delays, uncertainty or increased costs during a firm's failure.

We support a proportionate liquid asset requirement calibrated to realistic wind-down costs, the number and type of funds managed, operational complexity, retail exposure, outsourcing arrangements and the expected time needed to transfer or wind down management responsibilities.

The Panel believe that the FCA should require firms to evidence that liquid resources are readily available and not dependent on uncertain intra-group support.

42. How should capital and liquidity requirements interact for fund managers, and should a consistent standard for the quality of own funds and liquid assets apply, taking account of the typically simple nature of fund managers' firm-level balance sheets?

The Panel understand that the FCA is considering how capital requirements and liquidity requirements should work together and whether all firms should hold high-quality capital and liquid assets that are genuinely available when needed.

The Panel believes that consumers benefit if firms have both sufficient capital to absorb losses and sufficient liquidity to continue operating during periods of stress. One without the other may not adequately protect investors when problems arise.

Capital and liquidity requirements should be complementary. Capital should absorb losses and support redress, while liquid assets should ensure firms can meet obligations as they fall due and manage an orderly wind-down. For consumers, both are important: capital without liquidity may not be available when needed, while liquidity without adequate capital may not be sufficient to meet liabilities arising from misconduct or operational failures.

A consistent standard for the quality of own funds and liquid assets would improve comparability and reduce regulatory arbitrage, but it should be proportionate to the balance sheets of many fund managers. The FCA should focus on resources that are high quality, readily realisable, clearly owned by the firm. It should also require senior management to consider whether minimum requirements remain adequate in stress scenarios.

43. To what extent should structured risk management and wind-down planning expectations apply to fund managers, given that fund assets are held separately from the manager and do not count towards insolvency, and how should any such expectations be calibrated proportionately across firms of different sizes, complexity and risk profiles?

The Panel understands that The FCA is considering requiring fund managers to have more formal risk management processes and documented wind-down plans that explain how the business would continue essential functions or close in an orderly manner if it failed, and that requirements would be proportionate to firms' size and complexity.

Structured risk management and wind-down planning should apply to all fund managers, but with expectations calibrated by size, complexity, leverage, liquidity risk, outsourcing, operational dependence and retail exposure. In particular, the fact that fund assets are held separately from the manager does

not remove the risk of consumer harm. Poor planning can still result in delays, poor communications, disrupted valuations, suspended dealing, higher costs and uncertainty for investors.

The FCA could improve the proposal by setting minimum outcomes for wind-down planning, including timely consumer communications, continuity of critical services, treatment of vulnerable consumers where relevant, clear escalation triggers, transfer arrangements and testing of plans. Smaller firms should not be exempt from planning, but the documentation and testing requirements should be proportionate.

The FCA should also ensure that post-investment issues are not overlooked. Wind-down planning should include practical arrangements for complaints, redress, investor communications and continuity of oversight where something goes wrong, so that consumers are not left without clear routes to information, compensation or transfer of their investment.

44. What role should PII play within a prudential framework for fund managers?

Professional indemnity insurance (PII) can play an important role in protecting consumers by providing a source of funding for claims arising from negligence, errors or misconduct. However, PII should not be treated as a substitute for adequate capital, liquidity, governance or operational controls. Its effectiveness depends on policy scope, exclusions, limits, deductibles, claims history and the ability to make timely recoveries.

The Panel's previous view on external valuers is also relevant here. Valuation failures can create significant investor harm, and any prudential treatment of PII should avoid shifting valuation risk away from those best placed to control it. Where firms rely on external valuation expertise, both the valuer's liability and the manager's responsibility to act on concerns about inaccurate valuations should remain clear.

The FCA should allow PII to be recognised only where firms can demonstrate that cover is appropriate to the risks they run and the consumer harms that could arise. The FCA should also monitor whether exclusions or high deductibles undermine the value of PII, and should consider requiring firms to disclose in their internal assessments how insurance interacts with capital and redress planning.

If a firm's PII cover is not deemed adequate, the Panel supports the FCA's proposal to apply an additional PII capital requirement or a professional negligence capital requirement.

45. How could our data collection be improved, and where firms are subject to multiple prudential regimes, how significant are overlapping or duplicative reporting requirements?

Data collection should be improved by focusing on information that helps the FCA identify emerging harm to investors and market integrity, rather than on duplicative reporting that does not support supervision. Where firms are subject to multiple prudential regimes, overlapping reporting can increase costs that may ultimately be borne by consumers. The FCA should therefore seek to collect once, reuse where possible and align definitions across regimes.

The FCA should retain or replace existing notifications only where the resulting data gives supervisors an equivalent or better view of risks to investors. For example, information about acquisitions of non-listed companies, valuation reliance, investor concentration and overseas funds marketed into the UK may be important where those activities could affect retail consumers directly or indirectly.

The FCA could improve the proposal by publishing a reporting map showing how data submitted by firms will be used to identify consumer harm. It should prioritise standardised data on liquidity, valuation, leverage, investor concentration, complaints, redress, operational incidents, outsourcing failures and wind-down readiness. Reporting requirements should be proportionate but should not leave gaps where retail consumers may be exposed indirectly.

The FCA should be transparent with firms and wider stakeholders about how it uses supervisory data to assess risk. Publishing, at an appropriate level, the factors that inform the FCA's assessment of consumer-harm risk would help firms understand expectations and reduce incentives for regulatory arbitrage around thresholds.

46. What types of reporting would provide reliable indicators of potential or realised harm to fund investors or other market participants, including operational errors, redress events and near-misses?

Reliable indicators of potential or realised harm should include:

- operational errors,
- valuation errors,
- incorrect dealing prices,
- delayed redress,
- breaches of investment restrictions,
- liquidity problems
- suspensions or deferred redemptions,
- complaints trends,
- cyber or outsourcing incidents,
- conflicts of interest events and
- failures in investor communications.

The FCA should also use the information collected to share emerging sector-wide risks with firms in a timely and structured manner. Given its cross-market

supervisory perspective, the FCA is well placed to identify trends that individual firms may not detect. Appropriate feedback to industry would strengthen firms' own risk management and support earlier mitigation of risks affecting consumers and markets.

The FCA should ensure reporting captures not only financial loss but also consumer inconvenience, inability to access money, poor communications, unfair allocation of costs and the impact on vulnerable consumers where relevant. Firms should be required to report root cause analysis and remedial action, so that the FCA can identify patterns across the sector and require preventative improvements.

47. How could the prudential framework for CPMIs be designed to better reflect the nature of their combined fund management and MiFID investment activities?

The prudential framework for Collective Portfolio Management Investment firms (CPMIs)¹ should reflect the combined risks of fund management and MiFID investment activities without double-counting the same risk.

CPMIs may create consumer harm through both investment management failures and wider conduct or operational issues linked to MiFID services. The framework should therefore capture the full range of activities, client types, permissions, outsourcing dependencies, custody or client asset interfaces, and potential redress liabilities.

The FCA could improve the proposal by designing an integrated assessment that avoids duplication while ensuring no activity falls between regimes. For consumers, the priority should be that firms with multiple permissions hold resources appropriate to the total harm they could cause, maintain clear governance and can wind down in an orderly way across both fund management and investment services activities.

Where firms combine fund management with MiFID investment activities, the FCA should ensure that overseas arrangements are not used to weaken protections for UK consumers. Applying equivalent standards to firms marketing to UK consumers would support common understanding, reduce supervisory complexity and prevent regulatory arbitrage.

¹ A Collective Portfolio Management Investment firm (CPMI) is an FCA regulatory category for firms that carry out both fund management and MiFID investment services. A fund manager manages investment funds (such as UCITS or alternative investment funds (AIFs)) on behalf of investors. A MiFID investment firm provides investment services such as portfolio management, investment advice, dealing in investments or arranging transactions for clients.