

20 February 2017

Becky Young  
Competition Division  
Financial Conduct Authority  
25 The North Colonnade  
Canary Wharf  
London  
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Dear Ms Young

### **Asset Management Market Study, Interim Report**

The role of the Financial Markets Law Committee (the "FMLC" or the "Committee") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

The FMLC fulfils its role by liaising with legal and financial experts from both the public and private sectors in order to ascertain areas of legal uncertainty. Accordingly, the FMLC has established the Buy-side Scoping Forum to provide a space for the discussion of issues of legal uncertainty relevant to the buy-side industry.

On 18 November 2015, the Financial Conduct Authority (the "FCA") launched a market study of the asset management sector, with the aim of understanding whether there is effective competition in the asset management market, enabling both institutional and retail investors to derive most value. At a recent meeting of the FMLC Buy-side Scoping Forum, the Committee's attention was drawn to the interim findings of this study, published by the FCA in November 2016 in the Asset Management Market Study Interim Report MS15/2.2 (the "**Interim Report**").<sup>1</sup> The Interim Report sets out the FCA's initial assessment of the asset management market and proposes a package of remedies to boost competitive pressures in the market, thereby increasing the efficiency of the industry and attracting more investors.

The FMLC welcomes the FCA's initiative to address stakeholders' concerns about competition in the asset management market. While the FMLC recognises that the Interim Report is not intended to be a proposal for amendments to current regulation, it notes that a number of legal uncertainties arise from the analysis, in part owing to the high level of generality at which relevant terms are defined. The FMLC considers that a clarification of these issues at this interim stage of the study might aid the FCA in making its final recommendations.

### The definitions of "institutional investor" and "retail investor"

In reference to asset management market participants, the Interim Report identifies two distinct sets of clients: (i) "institutional investor", which is defined as "an investing legal entity which pools money from various sources to make investments"; and (ii) "retail investor", in which category all non-institutional investors are included.

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<sup>1</sup> The Interim Report is available at: <https://www.fca.org.uk/publications/market-studies/asset-management-market-study>.



The FMLC notes that these terms are not co-extensive with the categories of “client”, as defined in the FCA Handbook: “a customer or an eligible counterparty”. The Interim Report defines “institutional investor”, which is not defined in the FCA Handbook, broadly as “an investing legal entity which pools money from various sources to make investments”. It also lists, in Figure 3.2, categories of institutional investors including “pension funds, public sector, corporate, non-profit, sub-advisory, in-house insurance and third party insurance”, some but not all of whom will be *per se* eligible counterparties. This incongruence creates confusion as to how recommendations taken forward on the basis of feedback from the Interim Report will interact with existing regulation. Moreover, the listed categories in question are imprecise in many instances, resulting in a degree of additional uncertainty.

The FCA Handbook defines a “retail client” as “a client who is neither a professional client or an eligible counterparty” and it may possibly be inferred that “retail investor”, which is defined negatively as a “non-institutional” investor, in the Interim Report, means an entity that is a retail client of a firm but that is far from clear. Moreover, based on this broad categorisation, it is unclear whether “elective professional clients” (as defined in the FCA Handbook) should be classified as institutional or retail investors.

A degree of confusion results from the reliance which the FCA places on pooling in the definition of “institutional investor”. For instance, it is unclear whether the FCA intends to consider investments made by banks, insurers or large corporate entities on the basis of, respectively, deposits accepted, premiums collected or share capital raised as activities undertaken by institutional investors. This is of particular relevance since entities that collect money from multiple sources, such as a micro-enterprise established as a private limited company, could equally well themselves be regarded as retail investors.

Further uncertainty arises from the introduction in Figure 3.2 of “private clients” as a third category of investor, separate from the concepts of institutional and retail investor.

Section 10 of the Interim Report deals with proposed remedies. Several of these are said to be targeted specifically at retail investors, others are the subject of a feedback request concerning whether or not the remedies should be limited to retail investors. In this context, it is unclear whether the proposed remedies are to apply only to “retail clients” as defined in the FCA Handbook or to a broader category which might include, say, elective professional clients, as defined in the FCA Handbook. It would be helpful, in the view of the FMLC, if the FCA were to rely on previously-established definitions or to provide a more precise understanding of the investor categories.

#### Types of funds and segregated discretionary management mandates

There is a similar lack of specificity in the Interim Report with regards to categories of investment, which are listed exhaustively in paragraph 3.23 as: (i) pooled funds; and (ii) segregated mandates. Reference is made broadly to funds and fund managers without specifying whether this includes Alternative Investment Funds (“AIFs”), real estate investment trusts, venture capital trusts, collective investment schemes and/or collective investment undertakings, and their respective managers. The Interim Report defines a “segregated mandate” as “a fund that is run exclusively for one (institutional) investor” without acknowledging the existence of “funds of one”, which may be categorised for regulatory purposes as AIFs, collective investment schemes and/or collective investment undertakings.

The Report defines a “segregated mandate” as a “fund that is run exclusively for one (institutional) investor”. This is an imprecise description. There do exist “funds of one”, which may be categorised for regulatory purposes as AIFs, collective investment schemes and/or collective investment undertakings. An important part of the market, however, is made up of true segregated managed accounts, under which the assets are held on the balance sheet of the client, or by a custodian, and the manager is given a contractual mandate to exercise discretion over the composition of that portfolio from time to time. This is broadly the distinction between “collective portfolio management”, as defined in Directive 2011/61/EU on Alternative Investment Fund Managers (“**AIFMD**”) and segregated discretionary management within the meaning of Directive 2004/39/EC on markets in financial instruments (“**MiFID**”). It is unclear which of the FCA’s proposals are intended to be directed at segregated managers.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me to arrange such a meeting or should you require further information or assistance.

Yours sincerely,

A handwritten signature in black ink, reading "Joanna Perkins". The signature is written in a cursive style with a large initial 'J'.

Joanna Perkins<sup>2</sup>  
FMLC Chief Executive Officer<sup>3</sup>

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<sup>2</sup> The FMLC is grateful to Phil Bartram (Travers Smith LLP) and Leonard Ng (Sidley Austin LLP) for their assistance in drafting this letter.

<sup>3</sup> In view of the fact that this letter responds to an interim report issued by the Financial Conduct Authority, Sean Martin, Stephen Parker and Sinead Meany took no part in the preparation or drafting of this letter and it should not be taken to represent the views of the Financial Conduct Authority, HM Treasury or the Bank of England.