Hot topics for UK Wealth Managers

Autumn 2024

Contacts

Alex Ainley
Partner,
Financial Services Regulatory
T +44 20 7825 4248
E alex.ainley@simmons-simmons.com

David Hicks
Partner, Corporate
T +44 20 7825 4679
E david.hicks@simmons-simmons.com

Nina Obreshkova
Supervising Associate,
Financial Services Regulatory
T +44 20 7825 3876
E nina.obreshkova@simmons-simmons.com

Wealth management continues to be an exciting and dynamic sector, with significant consolidation continuing in an expanding regulatory landscape.

As the "retailisation of private markets" trend gains momentum, ensuring robust and reliable access for individuals is crucial. We're actively engaging with both the buy- and sell-side, discussing the current landscape, emerging products, EU/UK fund structures, global distribution via private wealth channels, and the challenges and regulatory changes in this rapidly growing area.

These topics draw from our experience of engaging with both clients and regulators on regulatory changes and providing advice to wealth and asset managers, and wealth management divisions of financial institutions, on how to navigate change as they grow and consolidate their businesses. We are seeing a lot of M&A and consolidation across the sector and are involved in numerous transactions, acting for both buyers and sellers, as well as supporting clients to manage consolidation, organic growth and adapting to regulatory change.

Please email or call us if you would like to discuss any of these topics further. We will be delighted to hear from you!

1. Strategy update from the FCA

On March 1 2024, the UK's Financial Conduct Authority (FCA) issued a portfolio letter with an interim update on its strategy in relation to the asset management and alternatives sector.

As you would expect, the FCA is keen as mustard on Consumer Duty price and value and also ESG, with the Sustainability Disclosure Requirements and investment labels regime coming into force in 2024.

A familiar theme that is once again voiced in the letter is valuations of private assets. With increased numbers of fund assets now in the form of private assets, the FCA wants valuations of those private assets to be reliable and robust. And so… a multi-firm review is in progress.

Other highlights include operational resilience, change management, and development of the government's Smarter Regulatory Framework (SRF) with a focus on MiFID, AIFMD and UCITS. The FCA has signalled its plans to 'lift and drop' significant parts of retained EU regulation but will take the opportunity to make changes to progress the three main priorities for reform:

- making the regime for alternative fund managers more proportionate;
- updating the regime for retail funds; and
- supporting technological innovation.

Simmons view: The FCA has been focused on change management and recently published its first substantial Final Notice in this area around implementation of the Market Abuse Regulation. There are lessons to be learned in this space around progressing action points promptly and clear internal communication.

In relation to private assets, the FCA is concerned about the risk of market disruption and the spectre of large write-downs if swathes of private assets turn out to be less valuable during a flight to liquidity. If this topic is relevant to you, revisiting your governance and valuation processes could be time well spent as the FCA gears up to launch its review.

2. The Consumer Duty

The Consumer Duty is a top priority for the FCA – it has ramped up its supervision of firms, with several of our clients receiving requests for information on how they have implemented the Duty.

We are currently advising over 50 clients on their Consumer Duty implementation, including major institutional asset and wealth managers, financial institutions, OPS firms and large insurers. The FCA's current focus is on engaging with firms on assessment of value (AoV) deficiencies. From 31 July 2024, the Consumer Duty has also applied to closed products and services and we helped a large number of clients prepare for the deadline. We set out some of the relevant considerations in our June 2024 Consumer Duty View.

In a move to ensure consumer protection, the FCA has announced a review in 2024 to assess the implementation of the Consumer Duty, focusing on price and value outcomes. The regulator has also published a helpful guide on its website, offering examples of good practice and areas for improvement. The guide, which is divided into six categories, is a valuable resource for firms working to embed the Duty.

In a series of 'Dear CEO' letters, the FCA has urged firms across different sectors to prioritize their reviews and take action in areas with the highest potential for harm. The asset management sector, despite receiving the shortest letter, is not exempt from these expectations, and price, value and transparency for consumers has been a particular focus within wealth management. In terms of price transparency, a key FCA hot topic recently has been to ensure that firms do not charge client money custody fees and also retain all or most of the interest on that money (so-called "double dipping").

Simmons view: Getting the Consumer Duty board report ready was an important focus this year and will continue to be on an annual basis. It will also be a focus for M&A processes and post-transaction consolidation, as risks with the approaches taken by a target business need to be assessed and potential differential models need to be reconciled and incorporated into the business of a wider group.

If you need a template or help with associated MI or integration planning, give us a shout!

3. Capital deduction for redress

The FCA is proposing tougher prudential requirements for personal investment firms (PIFs) to prevent consumer harm and reduce redress liabilities for the Financial Services Compensation Scheme (FSCS). The changes (which do **not** apply to MIFIDPRU firms) would require PIFs to quantify potential redress liabilities, allocate capital resources, and comply with an asset retention requirement. However, PIMFA has raised concerns about these proposals, arguing they could lead to unnecessary capital holdings and higher premiums for well-managed firms. The trade association is advocating for a more comprehensive prudential regime for PIFs, similar to MiFIDPRU firms.

Simmons view: These proposals are in part motivated by concern around historic advice to move out of defined benefit pension schemes. To date, significant amounts of compensation have been paid in relation to pensions advice and the FCA is worried that there is more to come.

While these proposals only impact PIFs (who are subject to the FCA's IPRU-INV rules), nevertheless the principle should be noted – your capital levels should reflect (amongst other things) the risks you face in terms of potential client redress for known issues. For MIFIDPRU firms, this would be captured in the ICARA process.

Defined benefit transfer advice has been a focus of M&A processes within the wealth management sector for some time, with an external compliance report often being commissioned as part of the sell-side planning. These changes will increase the spotlight on potential liability and feed into discussions on regulatory capital adjustments within pricing mechanisms.

4. Ongoing Advice Charge

In a webinar in December 2023, the FCA raised concerns that some consumers might be paying for services, such as annual reviews, that they are not receiving. The regulator is now focused on ensuring that customers are actually getting what they are paying for.

The FCA stated that it will contact several financial advisory firms to gather information about their ongoing services, particularly those for which clients continue to be charged. The FCA is interested in understanding if these firms have reassessed their services following the implementation of the Consumer Duty and if any changes have been made accordingly. This follows on from the Dear CEO Letter towards the end of last year, and well-publicised action through the Financial Ombudsman Service.

Simmons view: The FCA is on a data hunt, seeking information on client reviews and refunds related to the suitability of advice. This data will guide potential regulatory actions, with an update expected post-review. The regulator is surveying 20 of the largest advice firms, not out of concern, but to assess market practices. Previous letters from the FCA, including the Dear CEO letter last November, have highlighted concerns about the relevance, costs, and nature of ongoing services. Firms have been reminded of their duty to act in good faith under the incoming Consumer Duty.

Again, there is a principle here to take note of, namely that ongoing costs should reflect ongoing value being provided by way of service or product performance. While Consumer Duty brings this into sharper focus for retail clients, it can also be seen as part of a wider obligation to treat customers fairly.

This is an area that should be a key part of review and transitioning planning for any M&A process and consolidation of wealth management businesses within a group, including the potential impact on ongoing revenue and margins.

5. Advice Guidance Boundary Review – Closing the advice gap

The FCA and Treasury are jointly reviewing the line between financial advice and guidance to ensure consumers receive timely, affordable and effective help. The review aims to understand the current operation of this boundary and its impact on consumers, informing necessary changes. The paper identifies gaps where consumers want advice but are either unwilling or unable to pay for it, or are new to investing and unsure where to start. It also highlights a gap where firms wish to warn customers of potential risks but are worried about crossing the advice boundary.

There are three proposals for FCA-authorised firms which intend to bridge the gap between holistic advice and information and guidance:

Proposal 1: Further clarifying the boundary – this would result in greater certainty for FCA-authorised firms that they provide greater support to consumers without providing a personal recommendation.

Proposal 2: Targeted Support – a proposal for a new regulatory framework which enables firms to broaden the support they provide without explicit charges, based on limited information only. This would enable firms to suggest products or courses of action based on a target market the consumer has been identified as belonging to ("people like you"), rather than fully individualised support.

Proposal 3: Simplified advice - this proposal is aimed at enabling firms to better support those consumers who want to receive a personal recommendation when making a financial decision but for whom the more comprehensive support provided by holistic advice may not be cost-effective. This proposal comes following the feedback received from firms on the simplified advice regime proposed by the FCA in CP 22/24 - '*Broadening access to financial advice for mainstream investments*'.

Simmons view: the aim here is to set out early stage thinking about how greater numbers of retail clients can get helpful support and information without authorised firms having to take on the additional potential liability or unrecoverable expense associated with treating such advice as investment advice. It will be a delicate balancing act for the FCA in the post-Consumer Duty world and it is not easy to see how these proposals make it any more palatable for firms to go much beyond providing basic information if what awaits them is the full force of the Consumer Duty (regardless of the regulated activity status of the desired "advice").

For firms looking to expand through consolidation, it will be important to consider how differing approaches to classifying and providing advice to clients might raise issues and be reconciled and integrated.

6. Diversity & Inclusion

The Treasury, PRA, and FCA have responded to the TSC's Sexism in the City report, with the FCA prioritising non-financial misconduct, including sexual harassment and bullying. However, the previous Government showed limited commitment to the TSC's recommendations, rejecting expansions to the Women in Finance Charter and changes to pay gap reporting. However, a review was commenced of the whistleblowing framework and NDA legislation amid concerns they're being used to silence victims of discrimination and harassment.

Simmons view: the FCA's Policy Statement on Diversity and Inclusion in Financial Services had been expected in H2 2024 but the FCA has signalled that it is pausing its D&I proposals in order to take more time to consider the extensive feedback they received. In the meantime, the FCA proposes to proceed with its work on non-financial misconduct. It remains to be seen whether in due course the FCA will implement the proposed requirements for "large firms" (251 employees or more over a 3-year rolling average) which include setting targets to address underrepresentation, data disclosures and data collecting.

7. Prudential consolidation

We have helped a lot of clients with analysis of their prudential consolidation. Prudential consolidation is the grouping together of financial services firms and certain of their affiliated and connected entities for prudential regulatory reasons (i.e. it relates to the safety and soundness of financial services groups). It is not the same as accounting consolidation, although there can be a lot of overlap. Analysing and identifying the correct scope of prudential consolidation is important because it determines the relevant parent entity's regulatory capital, liquidity and governance requirements.

Prudential consolidation is an important topic when financial services groups acquire new entities or merge with other groups as it will need to be reworked and the implications of the acquisition/merger will need to be understood in advance.

Simmons view: prudential consolidation analysis can be very fiddly and is not always easy to get right. As well as needing to grapple with it in M&A situations, we have also come across situations where the analysis has not kept up with changes in a group over time and where capital and liquidity calculations require review. We would be happy to help you review your prudential consolidation if you have not done so for some time.

For additional information on our firm, please visit our website at **simmons-simmons.com.**

109876661