

How UK Proposals Would Simplify Fund Manager Regime

By **Leonard Ng** (April 28, 2025)

On April 7, HM Treasury published a consultation on regulations for alternative investment fund managers, or AIFMs.[1] On the same day, the Financial Conduct Authority published a call for input on the future regulation of AIFMs.[2]

This article discusses the key implications of the proposals for private fund managers, which set out a new approach to regulation of AIFMs in the U.K.[3]



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Proposed Changes to Scope of U.K. Regime

Current Regime

In the U.K., the current AIFM regulatory regime distinguishes between:

- Full-scope AIFMs: These are FCA-authorized and must comply with a comprehensive set of rules, including disclosure and reporting requirements, as well as stringent operating conditions.
- Small authorized AIFMs: These are authorized by the FCA, but not subject to the comprehensive requirements of full-scope AIFMs.
- Small registered AIFMs: These have simple registration with the FCA and are subject to limited reporting requirements. The small registered AIFM regime had been introduced to deal with firms that had not previously been FCA-authorized, such as managers of social entrepreneurship funds and registered venture capital funds.

Currently, the threshold for full-scope AIFMs is as follows:

- Over €100 million (\$114.8 million) of assets under management in leveraged assets, typically applicable to hedge fund managers; or
- Over €500 million of assets under management in unleveraged assets where there are no redemption rights for a period of five years, typically applicable to private equity sponsors.

Proposed Regime

In its call for input, the FCA has proposed a three-tier system of large, midsize and small AIFMs to replace the current regime. It is proposed that the applicable thresholds will be based on each firm's net asset value, i.e., an AIFM's assets minus its liabilities, rather than the existing test of leveraged assets under management, or assets under management, i.e., including assets acquired through the use of leverage, as follows.

Large AIFMs

The large AIFM category comprises net asset value of above £5 billion (\$6.7 billion). According to the FCA's data, this would capture 64 AIFMs from the current regime. These firms would be subject to a regime mirroring the current rules for full-scope AIFMs. However, in certain areas, such as disclosure and investor reporting, the FCA proposes to remove some detail where prescription is not needed to achieve the intended outcome.

The FCA notes that if the threshold were to be set at £10 billion net asset value, only 38 firms would be caught from the current regime.

Midsized AIFMs

The midsize AIFM category comprises £100 million to £5 billion of net asset value. The FCA anticipates that a significant number of existing full-scope AIFMs would be reclassified as midsized under the new rules. Based on the FCA's data, this tier would capture 463 firms from the current regime.

The FCA proposes that such firms would still follow the overarching rules and standards in the existing Chapter 3 of its Investment Funds sourcebook,[4] along with other AIFM Directive-derived standards in its senior management arrangements, systems and controls[5] and its Conduct of Business sourcebook.[6]

However, the FCA does not plan to impose more detailed procedural requirements, typically those in the Level 2 regulation, except where necessary.

Small AIFMs

The small AIFM category comprises up to £100 million of net asset value. It is intended for AIFMs in the early stage of development, or those that operate solely in a highly focused segment of the market.

Small AIFMs would be subject to core requirements appropriate to their size and activity, but the FCA does not expect that most existing small AIFMs will need to materially raise standards.

The move away from using leveraged assets under management to net asset value to calculate the relevant thresholds is interesting. The FCA notes in its call for input that net asset value is a more common measure of size used in the industry. As such, it may be easier for firms to understand than leveraged assets under management.

Although the FCA plans to remove the concept of leverage from the sizing thresholds, it notes that setting the threshold for large firms at £5 billion net asset value would, by default, capture most leveraged assets. The FCA call for input reiterates the FCA's focus on risks of high leverage in AIFs, and invites views on whether the FCA needs to be clearer about its expectations of risk management by highly leveraged firms.

The FCA uses the existing risk management rules to illustrate how the rules for AIFMs could be made more proportionate. For example, at a high level, the requirement to have a process for investment due diligence will only apply to AIFMs with AIFs investing in illiquid assets, and thus not for hedge funds investing in liquid instruments.

The requirement to set risk limits would only apply to AIFMs with significant leverage or liquidity mismatch. In relation to midsized AIFMs, it would only apply to those investing in transferable securities rather than private equity.

The U.K. government and the FCA are clearly taking deliberate steps to redesign the U.K. AIFM regime to make it more suitable for the U.K. market, with the aim of encouraging growth and competitiveness for the U.K.

The original European Union AIFM Directive framework was negotiated in 2010-2011, when the U.K. was part of the EU. As the second largest global asset management hub, with £14 trillion total assets under management, it is clearly appropriate that the U.K. should conduct a holistic review of the AIFM framework.

Note that the EU has itself already reviewed and revised its AIFM Directive, with the revised version required to be implemented in EU member states by April 2026.[7]

That said, this is really just the first step in terms of redesigning the regulatory framework for AIFMs. The key to a successful regime is to have an AIFM regulatory regime that operates seamlessly with the other two asset management pillars, that is, under the Undertakings for Collective Investment In Transferable Securities Directive, or UCITS,[8] and the Markets in Financial Instruments Directive, or MiFID.[9]

Indeed, with the U.K. no longer in the EU, there is no particular need to continue with the current trichotomy of investment managers having to be regulated rigidly as either AIFMs, UCITS management companies or MiFID portfolio management firms.

It appears that the U.K. government does not want to abolish those distinctions and build a brand-new asset management framework, which is understandable given the potential disruption, complexity and cost to business were it to do so.

However, the FCA should look at harmonizing where possible those rules that are currently inconsistent across each of those pillars, e.g., regulatory capital, remuneration, conflicts of interest and so on. Helpfully, the FCA call for input appears to indicate that the FCA is indeed looking for some consistency across the regimes.

Substantive Rules for AIFMs

The HM Treasury consultation and FCA call for input each also discuss a range of other issues that are of interest to private fund managers.

HM Treasury Consultation

Definition of AIF

HM Treasury does not intend to make any changes to the AIF definition or regulatory perimeter.

National Private Placement Regime

HM Treasury has proposed no changes to the national private placement regime, which relates to marketing by and of overseas AIFMs or AIFs.

HM Treasury notes that "[t]o date, market participants have not raised concerns" with the national private placement regime. However, that could simply be a function of the U.K. national private placement regime being relatively straightforward from a process perspective, as compared with that of many EU member states, to the extent that the

national private placement regime is available at all for overseas AIFMs.

The U.K. government should perhaps consider whether, from a policy perspective, the national private placement regime and marketing regime introduced by the AIFM Directive has achieved the correct policy outcome, as compared with the pre-AIFM Directive regime, which was more permissive in general.

External Valuation

Currently, external valuers are liable to an AIFM for any losses caused by the valuer being negligent or intentionally failing to perform its tasks. HM Treasury is considering whether growth in the market for external valuation services would be facilitated by removing the legal liability of the external valuer and removing this concept from legislation.

FCA Call for Input

Depositories

The FCA sees no immediate need to make radical changes to depositary requirements for large and midsize AIFMs, but welcomes input from stakeholders on whether the FCA should explore proportionate alternatives that meet global regulatory standards.

Remuneration

The FCA intends to review the operation and effectiveness of the remuneration rules for AIFMs, alongside the remuneration code for UCITS management companies and MiFID investment firms.

It is encouraging that the FCA appears to want to consider the remuneration rules for different types of managers holistically, across the AIFM Directive, UCITS and MiFID frameworks. In this regard, the FCA should also ensure that the remuneration framework for asset managers is consistent generally with changes made to the remuneration rules for dual-regulated firms, i.e., those regulated by both by the Prudential Regulation Authority as well as the FCA. For example, so-called small dual-regulated firms — under £4 billion of total assets, are now no longer required to comply with the rules on malus, claw back and buyouts.[10]

Prudential Requirements

The FCA intends to review the regime's prudential requirements and how they apply to firms of different sizes.

Some in the industry feel that the FCA could perhaps also consider whether the regulatory capital rules for AIFMs need to be updated in light of the changes to similar rules for MiFID portfolio management firms under the investment firm prudential regime.

AIFM Business Restriction

An AIFM is subject to the business restriction of managing an AIF, although it can obtain certain limited so-called top-up permissions to carry on other services, such as portfolio management for individual clients, as opposed to AIFs. This business restriction is being reconsidered as part of the FCA call for input.

One issue with the MiFID top-up permissions is that, while it allows an AIFM to carry on portfolio management activities, it does not allow an AIFM to engage in the MiFID activity of the execution of orders on behalf of clients. That restriction is problematic for some business models. For example, an AIFM would not be able to execute an order, even for an affiliate AIFM that makes a discretionary investment decision for the benefit of a fund.

Regulatory Reporting

The FCA wants to achieve a more effective reporting regime that is proportionate in its demands on firms.

Excessive reporting is often the key complaint made by regulated financial institutions. It is thus helpful that the FCA is focusing on making the reporting regime more proportionate.

Conclusion

Responses to the HM Treasury consultation and FCA call for input must be submitted by June 9. Following consideration of the responses, HM Treasury will publish a draft statutory instrument on the regulatory framework for AIFMs. The FCA also plans to consult on its detailed rules in the first half of 2026.

Overall, the proposals are a step in the right direction as the U.K. moves toward a more independent regulatory framework with regard to its own circumstances and aims following Brexit.

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[1] <https://www.gov.uk/government/consultations/alternative-investment-fund-managers-regulations-consultation>.

[2] <https://www.fca.org.uk/publications/calls-input/future-regulation-alternative-fund-managers>.

[3] The Proposals also contain proposals for listed closed-ended investment companies, which are not discussed in this article.

[4] <https://www.handbook.fca.org.uk/handbook/FUND.pdf>.

[5] <https://www.handbook.fca.org.uk/handbook/SYSC.pdf>.

[6] <https://www.handbook.fca.org.uk/handbook/COBS.pdf>.

[7] <https://eur-lex.europa.eu/eli/dir/2024/927/oj/eng>.

[8] <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02009L0065-20250117>.

[9] <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02014L0065-20250117>.

[10] PS16/23 – Remuneration: Enhancing proportionality for small firms.