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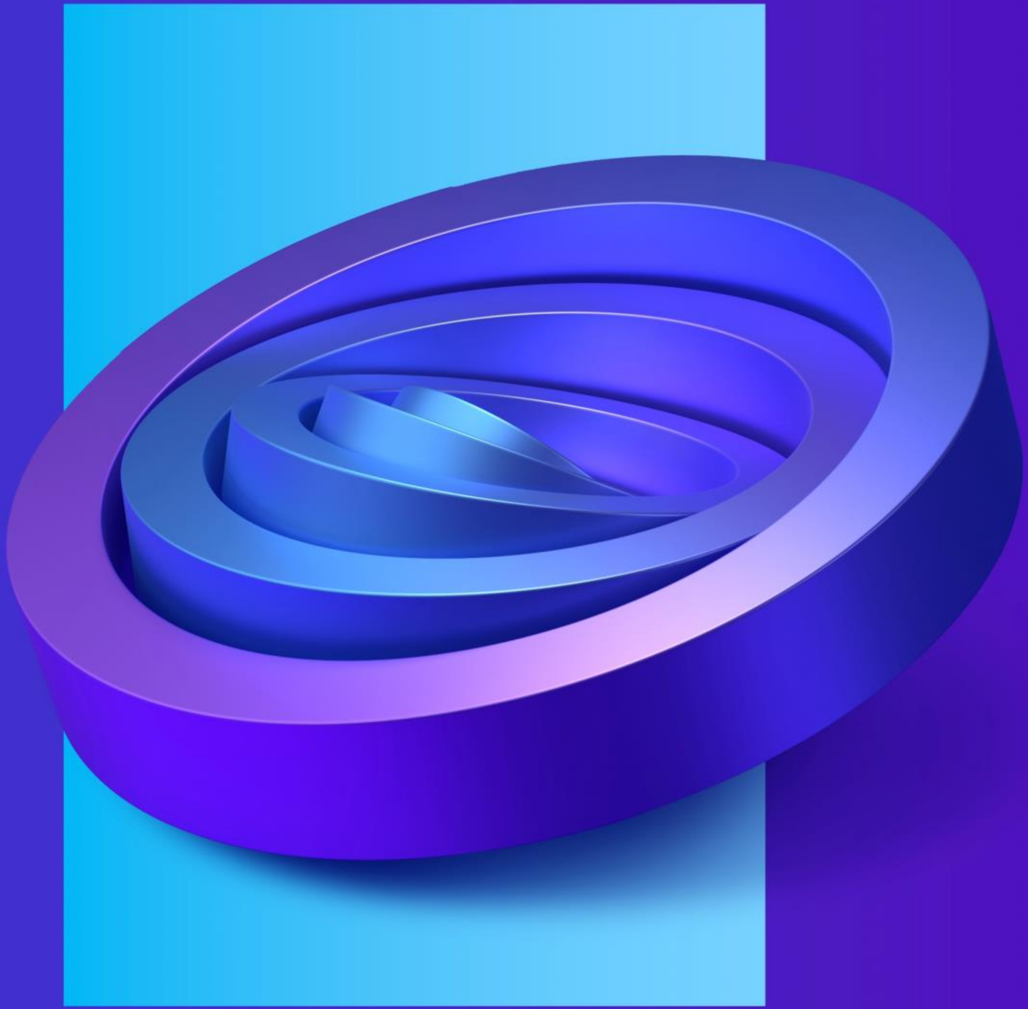
Building Resilience for the Future



Wealth and Asset Management Risk and ICARA Benchmarking Survey

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20 February 2025

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Foreword

> As regulatory focus moves from policymaking to supervision, and with economic growth a stated cornerstone of the FCA strategy through to 2030, we see firms prioritising digital innovation whilst embedding enterprise-wide resilience across their organisation.

Focus of the survey and key takeaways

As in previous iterations, the Risk Management and ICARA benchmarking survey for the Wealth and Asset Management sector focuses on three key areas:

- **Trends in Risk and Compliance functions:** we compare the different operating models implemented across Risk and Compliance functions and comment on how firms are reacting to broader changes across the industry.
- **Areas of regulatory focus:** we provide a deep-dive into four key areas of focus, focusing on digital innovation and AI, ESG and sustainability, Consumer Duty, and private markets.
- **Financial resilience:** as always, we benchmark the capital and liquidity requirements for wealth and asset managers. We also analyse the feedback firms have received from the FCA on their ICARAs and Wind-Down Plans since the IFPR came into force, identifying the areas of biggest focus by the FCA.

Trends within Risk and Compliance functions

Larger firms are more likely to adopt integrated Risk and Compliance functions overseen through a single reporting line into the CEO. Given the cost pressure the industry is under, we expect this Risk and Compliance operating model to become increasingly common as firms seek to drive efficiencies in the way they operate and see tangible benefits in housing operational and procedural aspects of risk management and regulatory compliance together in central teams.

Risk functions are also increasingly focussed on the impact of digitisation and disruptive technologies on their business. In reaction to this, there is significant focus on operational resilience and cyber skillsets in the Risk function. Firms are also using technology solutions (e.g. analytics tools, robotic process automation) to support efficient approaches to risk management oversight, with 75% of Asset Management CEO's say Gen AI is a top investment priority.

Regulatory change

With global geopolitical uncertainty and the UK government asking regulators for ideas to boost growth, we expect there to be significant changes in the nature and prioritisation of regulatory initiatives. Leading firms are leveraging technology to implement and manage this change efficiently.

Areas of regulatory focus

In 2025, regulators will continue with supervisory activity on priority areas, but they are at a crossroads from a policy perspective. UK and EU authorities are under pressure to deliver growth, and this is likely to increasingly factor into FS regulators' policymaking decisions.

On the other hand, regulators may remain resolute - maintaining and creating regulations that are judged to preserve the resilience of financial markets and protect investors. In this year's survey, we highlight four areas that we expect to be most impacted by changes in regulatory approaches.

Financial resilience and prudential regulation

Capital and liquidity requirements remain broadly consistent with those seen last year. For all firms in the survey, this is driven by operational risk requirements being a key driver of capital.

Now that the FCA has finished their first round of supervisory reviews under the new regime, there is a clear trend of the regulator focusing on operational risk assessments and wind-down planning. Where firms fell short in these areas, this often led to significant capital increases and additional regulatory scrutiny.

About the research

Our 2024 benchmarking approach

Our benchmarking survey, now in its tenth year, focuses on UK based wealth and asset management firms. This includes wealth managers, boutique and global asset managers, investment platforms and vertically integrated firms with services across all of this value chain. The participants range in size from small boutique asset managers through to the largest buy-side firms in the UK.

All firms included in our survey are prudentially regulated by the Financial Conduct Authority (“FCA”) and subject to the Investment Firms Prudential Regime (“IFPR”).

Participant background

This year’s survey is based on 33 participating firms of various scale as indicated by their assets under management, advice, or administration (“AUM/A”)[1].

11 participants manage assets in excess of GBP 200 billion while six firms have less than GBP 20 billion under management. In total, survey participants manage, advise or administer over £8.3 trillion of assets.

Acknowledgments

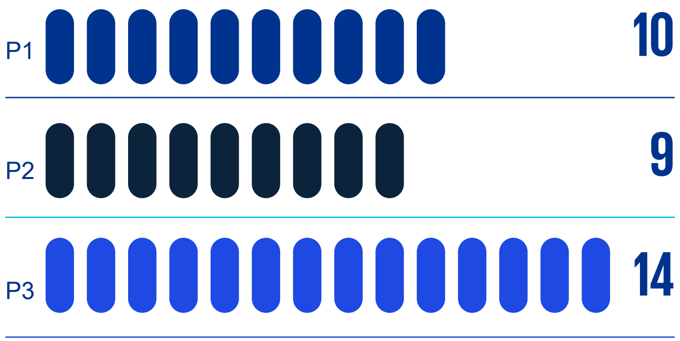
We would like to thank all of the firms that participated in the survey.

A special thanks to our survey team, Rob Crawford, Jack Machell, Hiren Tanna, David Collington and Michael Johnson.

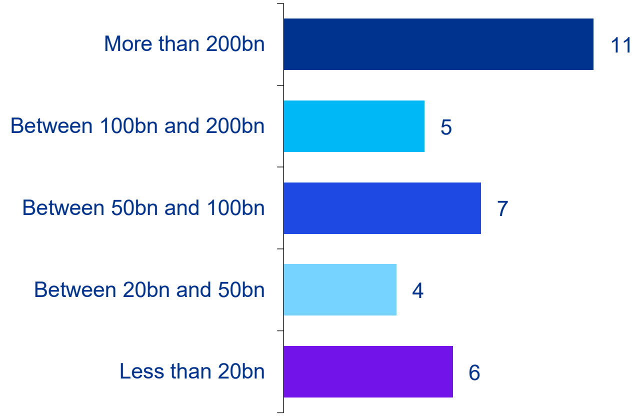
Daniel Barry

Partner

Number of Participating firms by Prudential Category



Number of Participating Firms by AUM/A (£)



> Our survey participants are responsible for over £8.3 trillion of assets under management, advice or administration. The range of their size and activities means the survey provides an industrywide view of the trends in Risk, Compliance and financial resilience across the sector.

[1] Note that throughout our report we use the term AUM/A to refer to the assets that each firm manages, administers or advises on. This includes AUM/A from both MiFID activities and also other regulated activities outside of MiFID (e.g. managing a UCITS) and is based on participant’s own definitions of AUM/A.

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Risk management and compliance trends

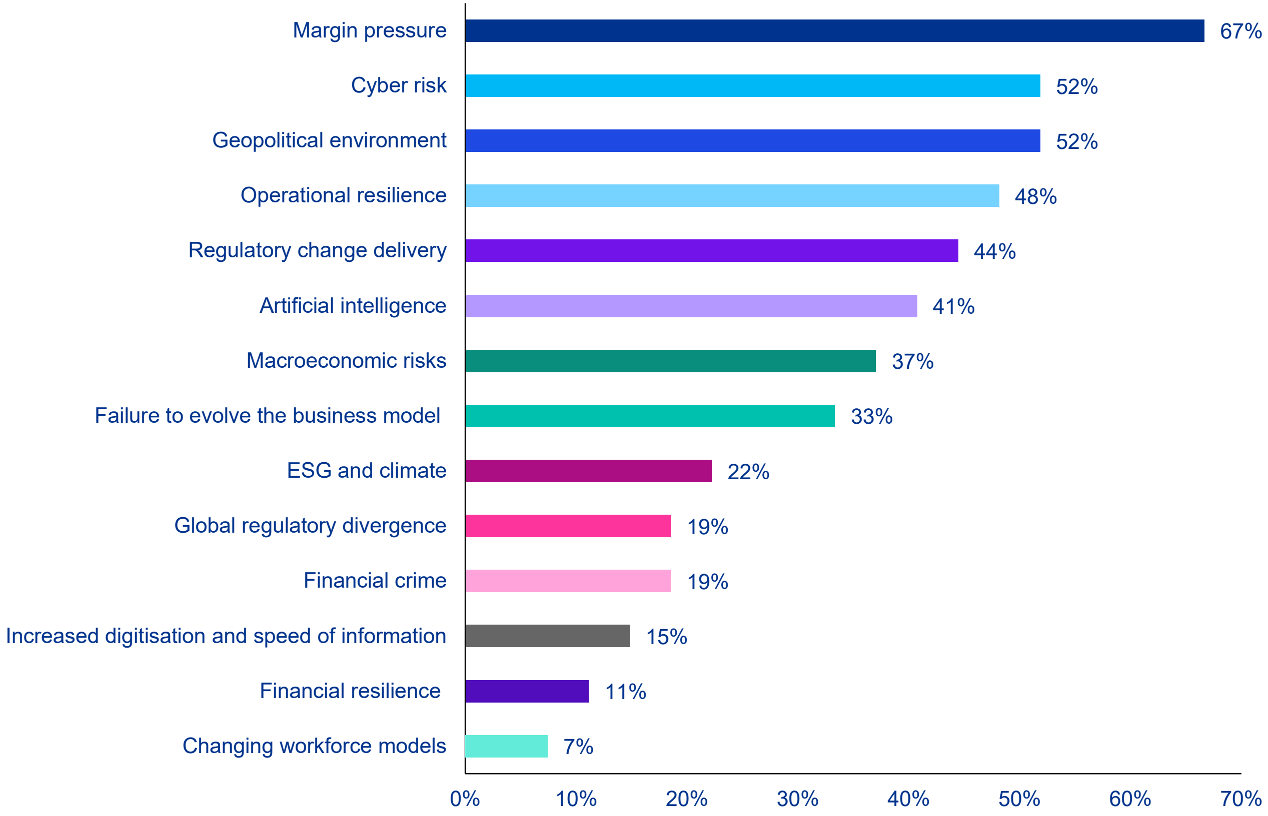
Impactful Risk Areas

The most impactful area of risk that firms are focussed on is margin pressure.

Trends in the data

- Key areas of focus for many firms are margin pressure (67%), cyber risk (52%) and the geopolitical environment (52%) where more than half of respondents see these as key areas of risk.
- Operational resilience (48%), regulatory change delivery (44%) and artificial intelligence (41%) are also top of firm agendas.
- While the geopolitical environment is seen a impactful, regulatory divergence (19%) is seen as less of a concern.
- Finally, ESG and Climate (22%) has dropped outside of the top 3 for the first time in a couple of years, and changing workforce models (7%) remains the least impactful area in responses.

Top 5 most impactful areas of risk for firms over the next three years
(percentage of respondents including the risks below)



KPMG View

Margin pressure is having a significant impact across the Wealth and Asset Management sector. Revenues under pressure due to external pressures to reduce fees, particularly for active asset managers. Costs are also rising as firms invest in technology, infrastructure and people. In response to this, many firms are undertaking cost optimisation strategies and looking for ways to diversify their product and asset class offerings.

Cyber risk will continue to feature towards the top of the risk list given the on-going adoption of cloud strategies, digital platforms and transformation programmes, increased online servicing and a range of third-party risks – strengthening cybersecurity infrastructure is seen as a key priority.

Geopolitical risks have evolved significantly with exposures changing at a rapid rate.

We expect AI to continue to move up the risk agenda (last year it was not on the agenda of most firms). We can already see that firms are implementing AI initiatives and regulators are focussing on this area. Model risks, a lack of transparency, data biases and the correlation with cyber risk mean that we expect managing AI related risks to be a real challenge in the next three years.

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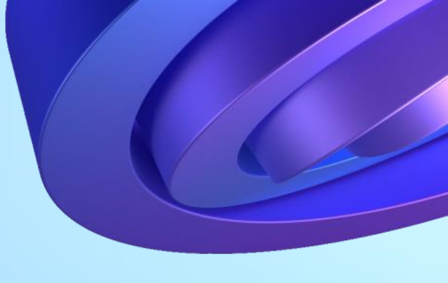
Design of Risk and Compliance functions



Many firms are continuing to develop and enhance their Risk and Compliance operating model. Some use first line resource to support their wider risk and compliance functions.

Trends in the data

- 44% of participants operate standalone Risk and Compliance functions, with different reporting lines into the CEO and Board.
- Larger firms are more likely to operate Risk and Compliance as a fully or partially integrated function. Whereas smaller firms are more often implement standalone functions.
- 66% of participants have implemented an operating model with dedicated risk resourcing in the first line of defence. While only 32% of participants operate a dedicated first line compliance function. With larger firms more likely to utilise first line Compliance resource.
- Year-on-year more firms are using first line resource to deliver Risk and Compliance activities.

Design of Risk and Compliance functions
(percentage of firms adopting the following approaches)

44% Standalone functions

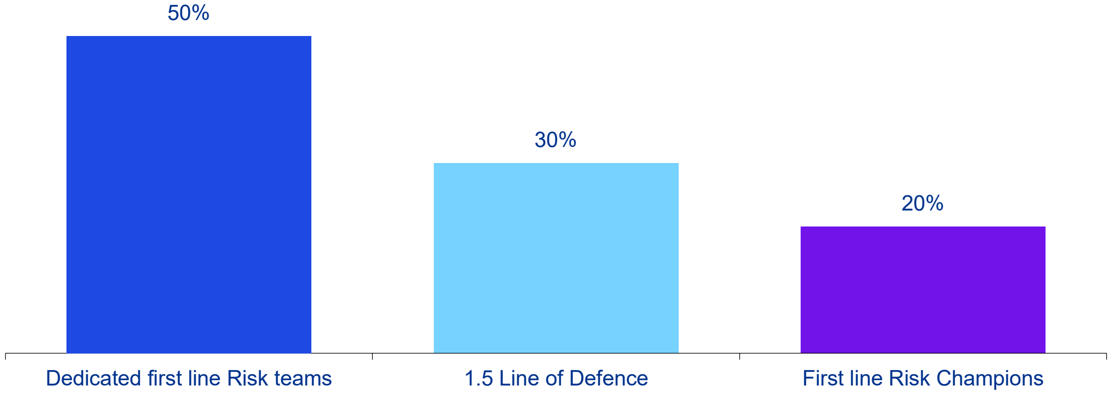
26% Fully integrated functions

30% Partially integrated functions

66% have risk resource in or supporting the first line

32% of firms have Compliance resource in the first line

Approaches to operating with first line Risk and Control functions
(percentage of firms adopting the following approaches)



KPMG View

There is no universal approach to the design of Risk and Compliance functions, however, there are consistent drivers for change across the industry. Many Risk and Compliance functions continue to be challenged by the business to "do more with less". This push has led many firms to consider how to improve the operating efficiency of their teams and how new technologies may enable a more streamlined operating model.

In our experience, firms are taking the following steps to react to these drivers for change:

- **Increased first line involvement:** Larger firms are increasing the number of first line resource, and their Risk and Compliance functions are more likely to delegate additional activities to the first line.
- **Integrated functions:** A majority of firms surveyed have looked to integrate at least some aspects of Risk and Compliance activity. Aiming to streamline reporting structures and reducing governance overheads are noted as key drivers.
- **Greater appetite for new technologies:** Nearly all firms surveyed are actively exploring which new technologies would provide the greatest benefit across Risk and Compliance.

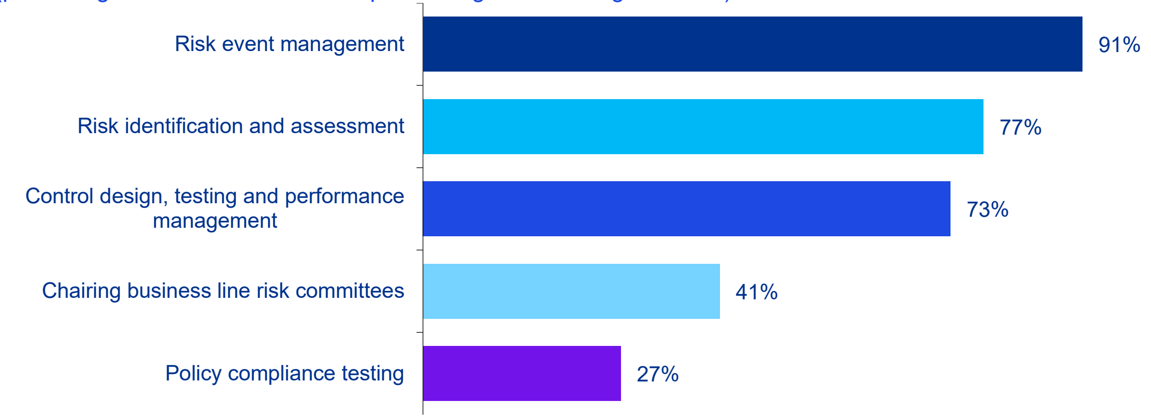
First line responsibilities for Risk and Compliance

Firms are using First Line Risk and Compliance teams to own key activities in these area and to support the business in meeting their obligations

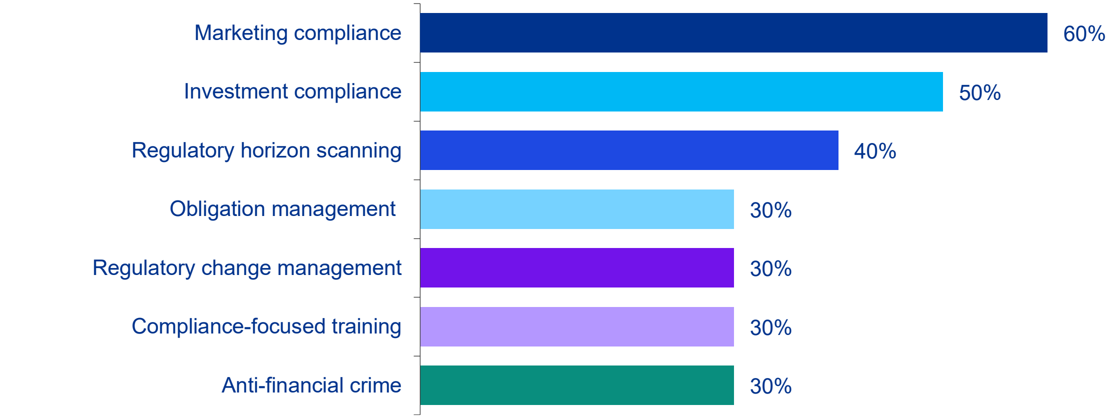
Trends in the data

- Where participants have formal first line Risk resource, the most common activities they perform are risk event management (91%), risk identification and assessment (77%), and control design, testing and performance management (73%). This is broadly consistent with the activities these teams performed in previous years.
- Approaches to first line Compliance functions vary, with marketing compliance (60%) and investment compliance (50%) being the most common activities sitting in the first line.
- Activities like regulatory change management (30%) and obligation management (30%) are being delivered by some first line Compliance functions, which continues the trend of activities that would traditionally be delivered by the second line, moving into the first line.
- Compared to previous years, the size of firms first line Risk and Compliance teams are increasing. The increased adoption of this approach indicates that firms are benefiting from increased first line involvement.

Most common activities performed by first line Risk teams
(percentage of first line Risk teams performing the following activities)



Most common compliance related activities performed in the first line
(percentage of first line teams performing the following activities)



KPMG View

As firms look to enhance how resources are used within their Risk and Compliance functions, it is becoming more common for additional responsibilities to be transferred to the first line. In our experience, this transition to the first line is typically paired with broader risk transformation activities which deliver a wholesale shift in the way in which Risk and Compliance activities are performed, underpinned by implementation of new technologies.

Maintaining dedicated first line resource can lead to a more robust and consistent approach to Risk and Compliance through a more embedded approach to these areas. Where we see firms that have successfully implemented this approach it is supported by clearly delineated reporting lines and ongoing validation to ensure an appropriate balance between first and second line.

Where this approach has been a success, it often leads to additional activities being transferred over time (for example, regulatory change management). This enables the second line to focus on independent oversight and challenge to the business on these areas. We expect this trend to continue as the operating models of firms mature.

Headcount across Risk and Compliance functions and in-demand areas

Headcount across Risk and Compliance teams scales with AUM/A and assets managers have significantly higher headcount in Risk functions due to the size of their Investment Risk teams.

Trends in the data

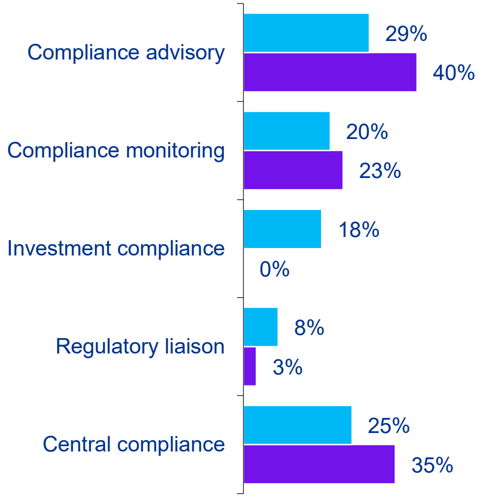
- Asset managers dedicate a significantly proportion of their overall risk FTE to investment risk management (42%). This creates a significant structural difference between asset managers and other buy-side firms.
- Firms who have no investment risk team are far more likely to have significant resources in enterprise risk (48% of FTE) and non-financial risk (39% of FTE) areas.
- Similar trends exist within Compliance functions, with compliance advisory and central compliance teams receiving more proportional resource compared to investment compliance teams.
- The impact of these differences is that asset managers have significantly higher headcount across Risk and Compliance than other firms in the survey. With all things being equal, we have observed around a 40% FTE uplift amongst these firms.

Headcount of Risk and Compliance functions
(average FTE across first and second line Risk and Compliance functions)

64	14	37	59	71	95
All firms	Less than £20bn	Between £20bn and £50bn	Between £50bn and £100bn	Between £100bn and £200bn	More than £200bn

Proportional headcount across Risk functions

Proportional headcount across Compliance functions



Participants with investment risk teams
Participants without investment risk teams

KPMG View

Where smaller firms operate with leaner Risk and Compliance teams, they are more likely to be made up of experienced generalists as they must cover multiple areas of Risk and Compliance. However, this can create key person dependencies and limit their ability to challenge the first line on complex technical areas. Therefore, these firms are still likely to recruit for specialist skillsets in key areas (e.g. cyber) or to obtain external third-party support on these key risk areas. The economies of scale that larger firms have in this area typically leads to significant benefits in being able to recruit and retain the right second line skillset.

While the core activities of Risk and Compliance functions are not surprising, it is notable that some firms are able to deploy resource into areas that can provide significant benefits. For example, a regulatory liaison team in Compliance can be critical to maintain good relationships with regulators. As more firms move responsibilities into the first line, there is an opportunity for Risk and Compliance leaders to adopt a more strategic approach to their own functions and activities.

We are seeing an increasing number of firms out-sourcing or off-shoring certain Risk and Compliance activities in fashion normally associated with banking groups. Whilst this is typically reserved for the larger managers, we see surveillance, aspects of compliance monitoring and control testing being undertaken in lower cost locations or by trusted partners who can operate services at scale.

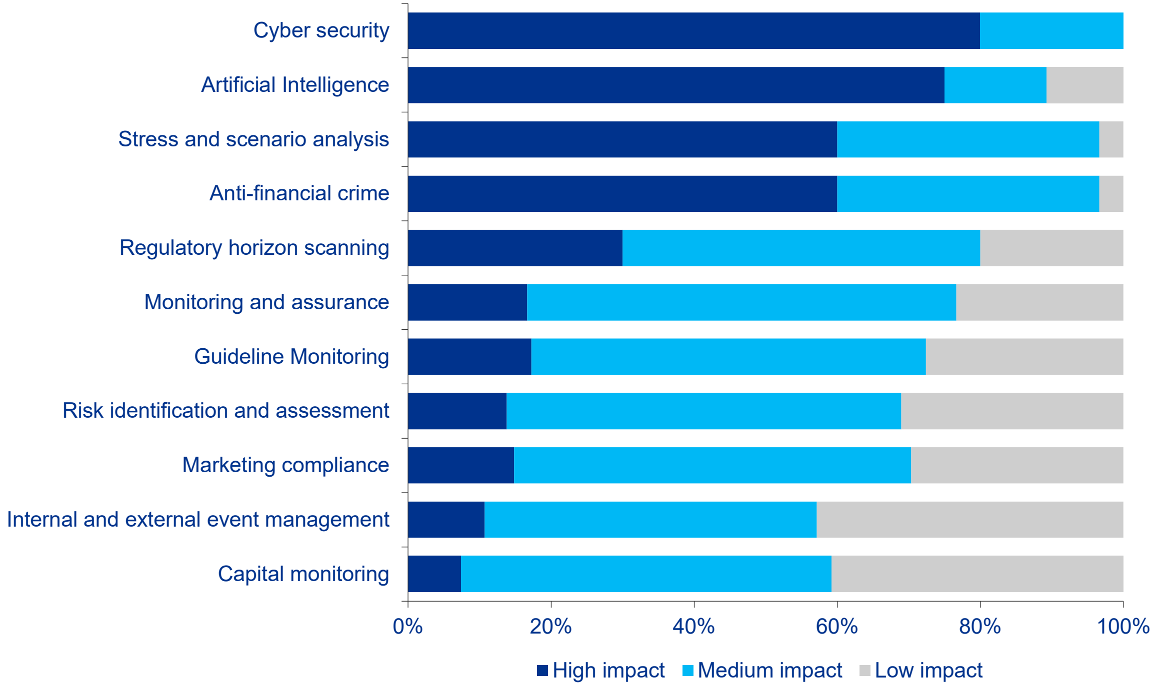
Technology risks and adoption of technology in Risk functions

Participants expect cyber security and financial crime risk processes be significantly impacted by digitalisation and disruptive technologies.

Trends in the data

- For the third year in a row, cyber security ranks as the highest area firms expect to be impacted by digitisation, with 80% of firms expecting it to have a high impact on their business. Artificial intelligence (70%), stress and scenario analysis (60%), and anti-financial crime (60%) are also highly rated by participants.
- 93% of participants use a Governance, Risk and Compliance (“GRC”) system. 20% of firms surveyed plan to migrate to a new GRC system, with a further 12% exploring a migration in the near future. 24% of firms are planning to make significant enhancements to their existing GRC tooling.
- Nearly 70% of firms are considering implementation of new technologies within Risk and Compliance, with cloud-based analytic solutions, AI and machine learning, and process automation key areas of focus.
- Over 20% of firms are exploring the deployment of AI and machine learning tools within their Risk and Compliance function.
- The Top 3 most widely used technologies in Risk and Compliance functions involve some form of cloud data storage (38%), internal data analytics tooling (40%)
or an external data tooling (38%).

Areas of risk management that firms expect to be impacted by digitisation and disruptive technologies



Top three emerging technologies in Risk and Compliance functions

01 Externally developed analytics solutions	**02** Robotic Process Automation	**03** Artificial Intelligence and machine learning

KPMG View

Cyber risk will continue to be an area of significant focus for all firms. The nature of the risk landscape and pace of technology change both in firms and externally means that many feel this risk is constantly evolving.

There are many third-party service providers who advertise end-to-end solutions for cyber risks. Where these services are used, firms benefit from having an experienced Risk team who can appropriately challenge and refine the approaches adopted by the third-party provider.

Each year, an increasing number of firms have begun to use more advanced technologies within their Risk and Compliance functions. However, with many firms migrating to new GRC tools or considering a change in vendor, this shows that all technology used in in Risk and Compliance functions continue to evolve. Migrating to new GRC systems can be very challenging, however, this also provides an opportunity for significant transformation in the design and operating model of Risk and Compliance.

Leading firms are also seeking to automate manual processes in these tools. The most significant driver for the adoption of new technologies is the perceived productivity benefits that they bring, especially when Risk and Compliance functions are under cost pressure.

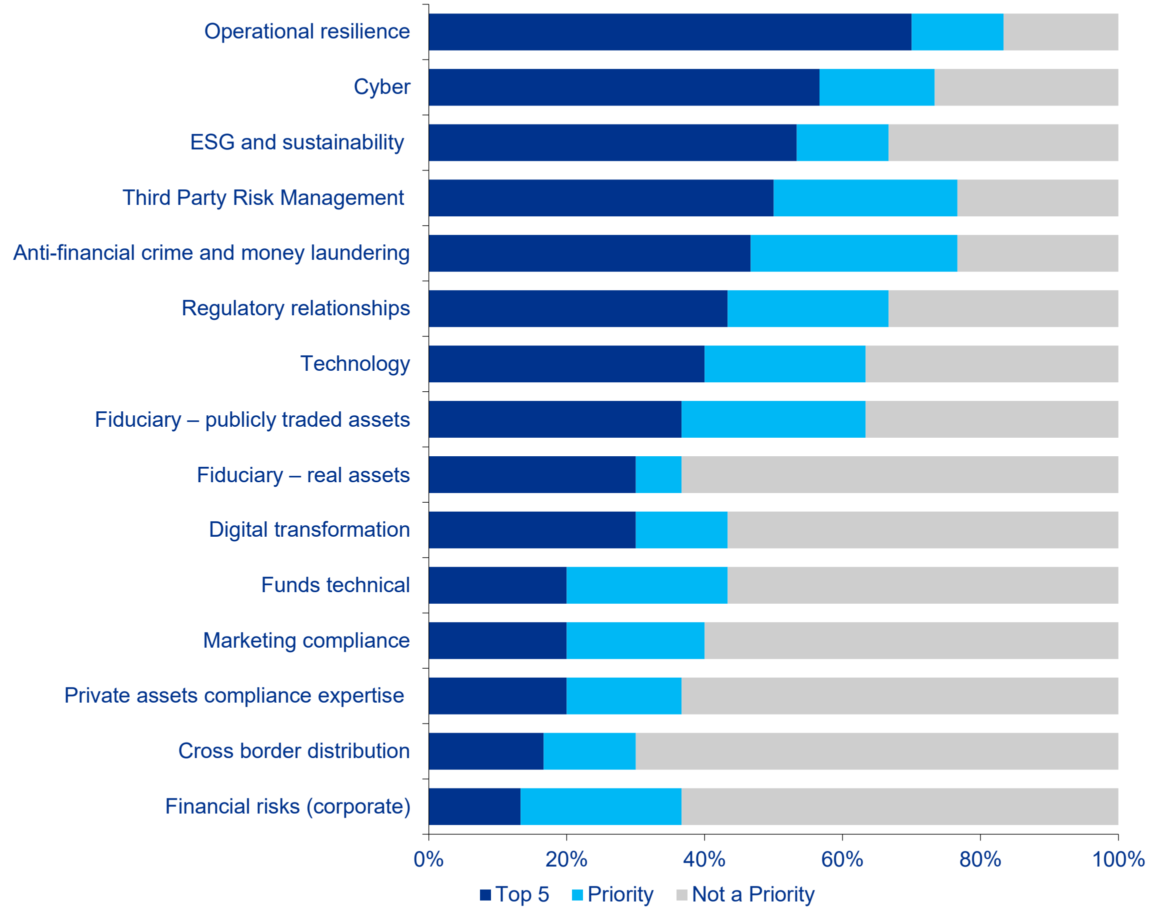
Skillsets

Specialised skillsets in Risk and Compliance functions are in high-demand.

Trends in the data

- 80% of participants reported that operational resilience was a priority area within their Risk and Compliance functions.
- Other regulatory driven topics, like ESG and sustainability (63%) and anti-financial crime (77%), also rank highly. This is a trend we have observed in recent years, with many firms requiring specific resourcing and support due to emerging regulations.
- More traditional skillsets, like corporate financial risks (33%), cross border distribution (30%), and marketing compliance (40%), are less in-demand compared to recent years. In fact, a majority of firms have reported that these areas are not a priority for them.

Most in-demand skillsets within Risk and Compliance functions



KPMG View

In KPMG's recent CEO outlook survey, 89% of Asset Management CEOs surveyed said they plan to increase headcount across their business. We expect this to also result in increased headcount Risk and Compliance functions.

As new regulations and requirements are introduced, there is a natural trend for related skillsets to become more desired. This is particularly the case where the requirements in these areas are significant (such as for operational resilience) and where regulatory requirements vary across jurisdictions (such as for ESG). These factors are likely the main reasons that operational resilience and ESG and sustainability skillsets are some of the most in-demand across the industry.

Recruiting to these roles can be difficult when the same specialists can also use their skillset in first line activities. However, we have observed some firms successfully develop and design second line activities and operating models in these areas to enable them to attract and retain talent.

It is interesting to see more technical, asset class and product specific skillsets being less in demand which doesn't necessarily align to what we see on the wider growth agenda for innovative products like ETF's or the noted growth in private credit, as an example.

02

Evolving areas of regulation

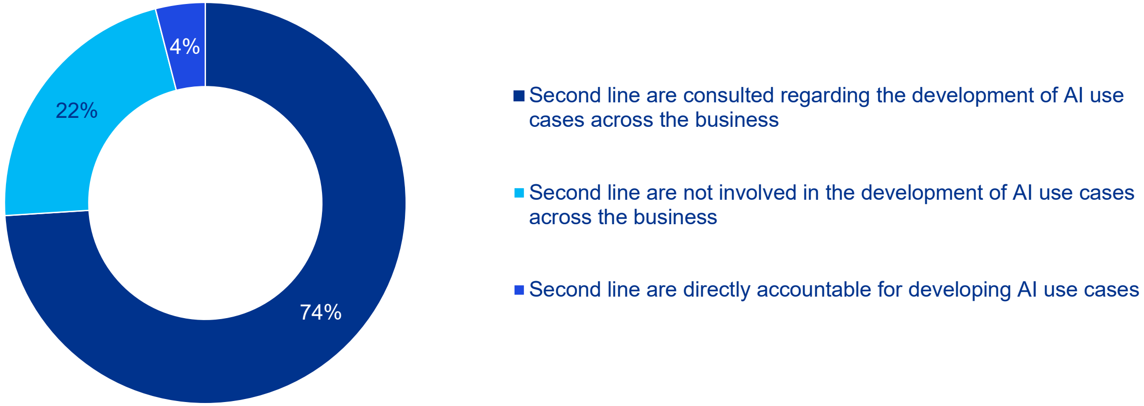
Digital Innovation and AI

With many participants looking to take advantage of advancements in AI, Risk and Compliance functions have had to react quickly to ensure that risks inherent to newly deployed technologies are managed appropriately.

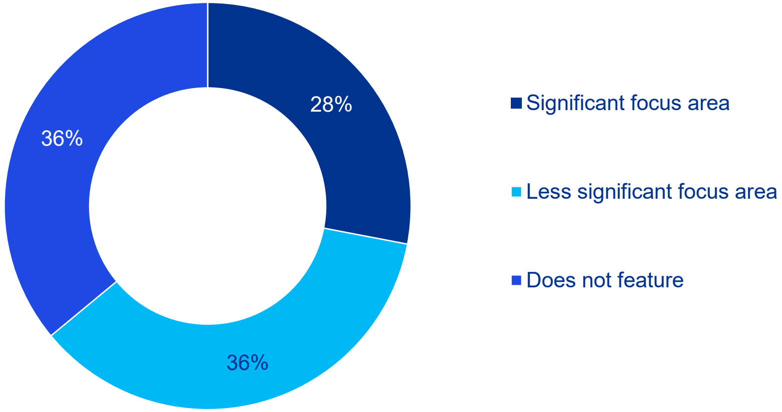
Trends in the data

- A majority of firms have adopted similar approaches regarding the involvement of their second line in the development of AI use cases. Over 70% of participants consult the second line, with only 4% holding the second line directly accountable for developing use cases. Surprisingly, 22% of firms have reported that their second line of defence are not involved in AI use case development at all.
- 36% of firms reported that the emergence of AI does not feature in their second line monitoring and assurance programmes. Only 28% of participants consider this to be a significant focus area.
- 62% of firms reported that they do not plan on carrying out an AI-focussed compliance monitoring review over the next year.
- Only 35% of firms expect to be in scope of the EU AI Act.

Role of Second Line Risk and Compliance in AI use case development



Emergence of AI in Second Line Monitoring and Assurance



KPMG View

In KPMG's recent CEO outlook survey[1], 75% of Asset Management CEOs surveyed said that AI was a top investment priority for their firm. Understanding how best to deploy this potential investment and ensuring that the risks associated with the deployment of AI are managed appropriately is a key focus area for risk leaders.

Most firms surveyed ensure that second line is consulted during the development of AI use cases. Second line involvement should help ensure that AI use cases are compliant and are aligned with delivering good outcomes for investors and that second line can implement the required processes and procedures to manage any risks associated with the deployment of AI across the business.

Leading firms are also considering the emergence of AI as part of second line monitoring and assurance reviews. For a quarter of firms AI is a significant focus. Of these firms, many have already either trialled or fully deployed AI-based technologies within their business.

Typical use cases for second line teams in the sector centre around automated commentary and analysis for reporting, dynamic connectivity of evolving regulatory footprint to impacted policies, risks and controls, and Investment Management Agreement (IMA) change detection and updates.

ESG regulatory change

For many participants, the implementation of the FCA's Sustainability Disclosure Requirements ("SDR") has been a significant area of focus.

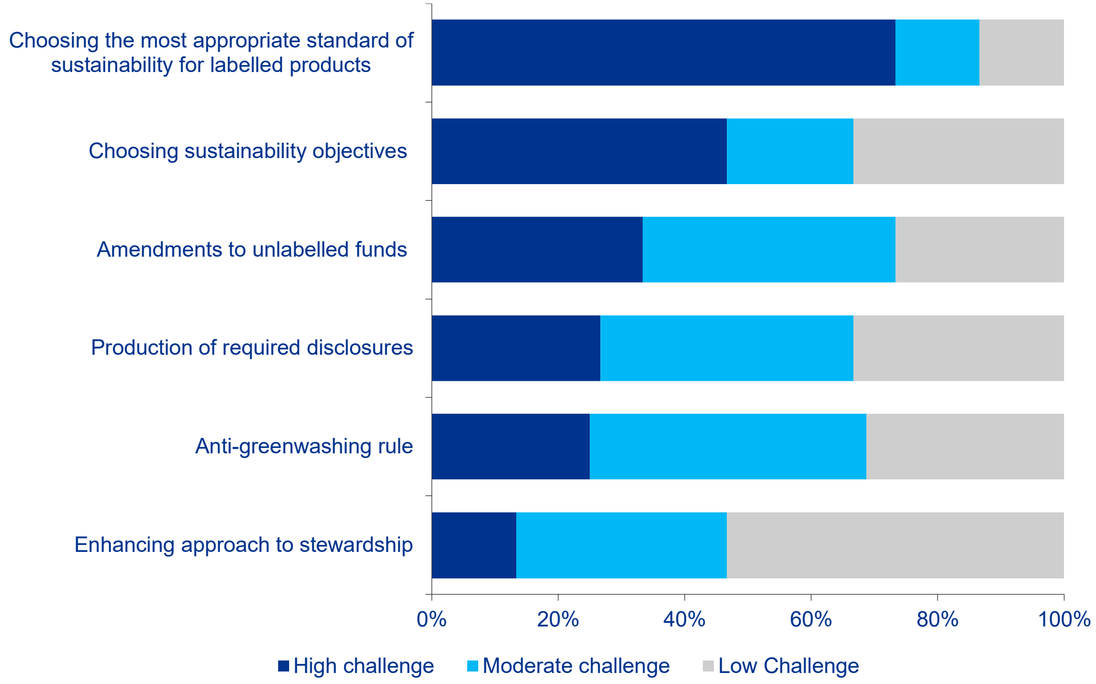
Trends in the data

- 59% of in-scope participants are planning to label at least one fund under the SDR in the 12 months to November 2025.
- Over 80% of firms expect to label less than 10% of all funds that are in-scope of the SDR. On the other hand, around 15% of firms expect to label more than 20% of in-scope funds. Some leading firms are planning to label over 40 funds.
- The "Focus" label is expected to be the most widely used SDR label, with 62% of firms reporting that they expect to use this - significantly more than any other label.
- 60% of participants expect to be captured by the FCA's extension of the SDR to portfolio management.
- Only 15% of firms expect to make any significant changes to their product range as a result of SDR or ESMA's fund name guidelines.
- 73% of participants reported that developing a sustainability standard for labelled products was a significant challenge when implementing SDR. Developing sustainability objectives for labelled products (47%) was another challenging area.

Which SDR label is expected to be used most by participants?

62%	15%	15%	8%
Focus	Mixed Goals	Improver	Impact

What would you say has been the most challenging aspect of SDR implementation?



KPMG View

Surveyed firms expect to apply an SDR sustainability label to at least one of their UK funds in 2025. However, most are only planning to label a small proportion of their in-scope fund range.

Most firms are looking to adopt SDR labels for a subset of funds, before potentially rolling out a more expansive approach.

There may be some level of first-mover advantage for firms that are actively launching multiple labelled funds. However, it seems that only a small proportion of firms are taking steps to capture this.

Where firms are using SDR labels, the most significant challenge relates to developing an appropriate sustainability standard. The FCA has not provided extensive clarity on its expectations, and many firms have found the approval process for labelling-related fund changes to be challenging.

As a result, some firms have adopted a 'wait and see' approach, and are planning to launch labelled products only after more information is available about how market leaders in the space have approached product labelling.

The FCA was expected to publish final rules on extending the SDR regime to portfolio managers in Q2 2025 – however, this has now been delayed again.

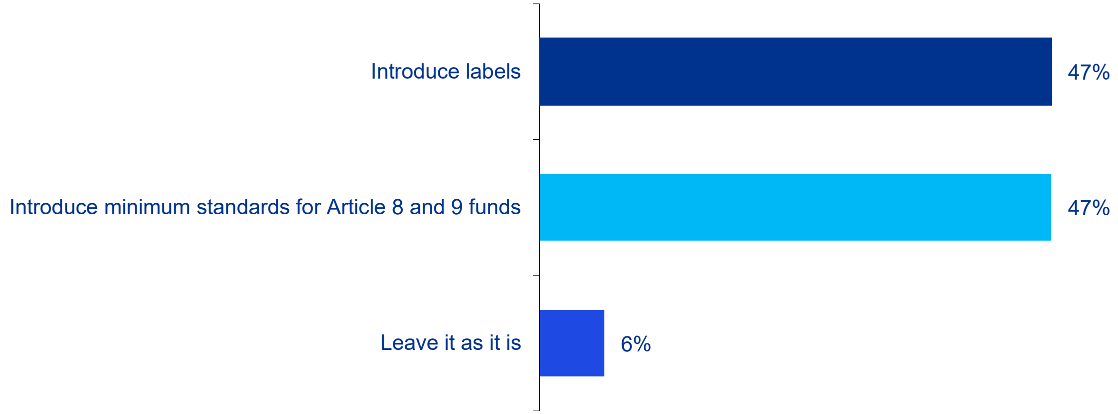
ESG regulatory change

Most respondents believe the EU Sustainable Finance Disclosure Regulation (SFDR) could be improved.

Trends in the data

- Only 6% of participants believed that the SFDR did not require reform. Other responses were evenly split over the most appropriate way to reform the SFDR.
- Nearly half of the firms in our survey (47%) supported the introduction of labels to improve the SFDR. The same number also supported the introduction of minimum standards for Article 8 and 9 funds.

Participants' views on the most appropriate way to reform the SFDR

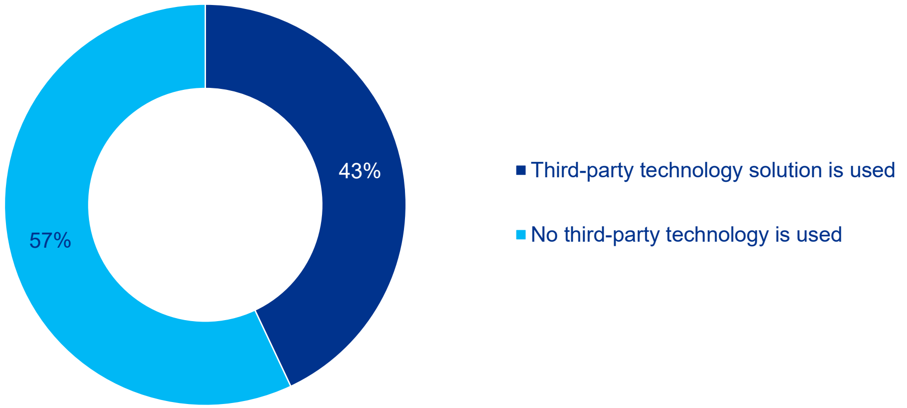


Over 40% of firms use some form of third-party technology to support their ESG reporting activities.

Trends in the data

- A growing number of firms are utilising third party technologies to deliver ESG reporting activities. We expect this trend to continue as more third-parties look to introduce specific products to aide firms.

Adoption of third-party technology solutions to support ESG reporting activities



KPMG View

While the UK's SDR regime is still in its infancy, the EU's SFDR has been in place for several years. However, challenges around its interpretation, and questions around whether it is delivering on its goals, have led to proposals to revise aspects of the rules.

While our survey results indicate the potential to improve the SFDR, they also show the diversity of views on how this should be done in practice.

The introduction of sustainability-related disclosures under a variety of regimes, and their ongoing revision, has been a significant burden in recent years. Many firms will feel that the benefits of any enhancements to the regime, will be outweighed by the costs of changes, particularly as they try to embed reporting into BAU processes.

So far, technology adoption to support sustainability reporting has been somewhat limited, with fewer than half of participants currently relying on third party technology solutions to help facilitate and automate the reporting and disclosure process. This is likely to change as emerging sustainability reporting requirements, such as CSRD, impose mandatory assurance requirements on sustainability disclosures. Many firms are seeking to use technology to enhance the governance and controls around sustainability disclosures to minimise the risk of receiving an adverse assurance opinion.

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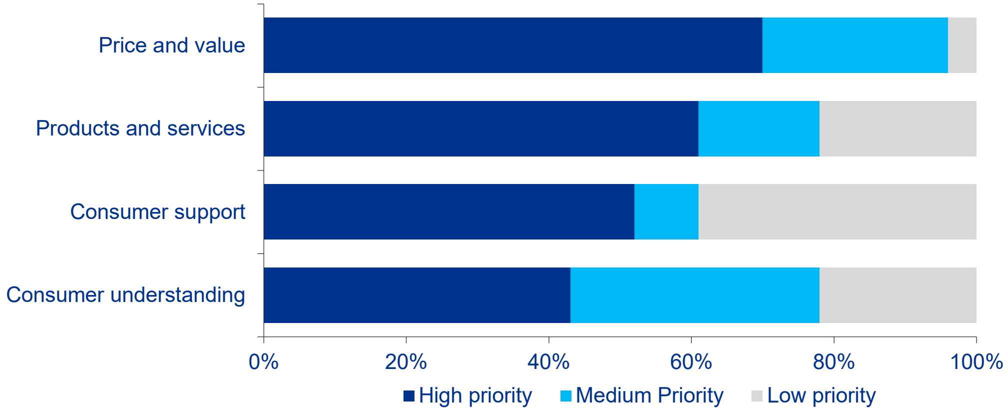
Consumer Duty

More than 18 months on from the implementation of the Duty, the FCA has moved on from assessing implementation to intervening on specific topics and practices where it wants to see improvements.

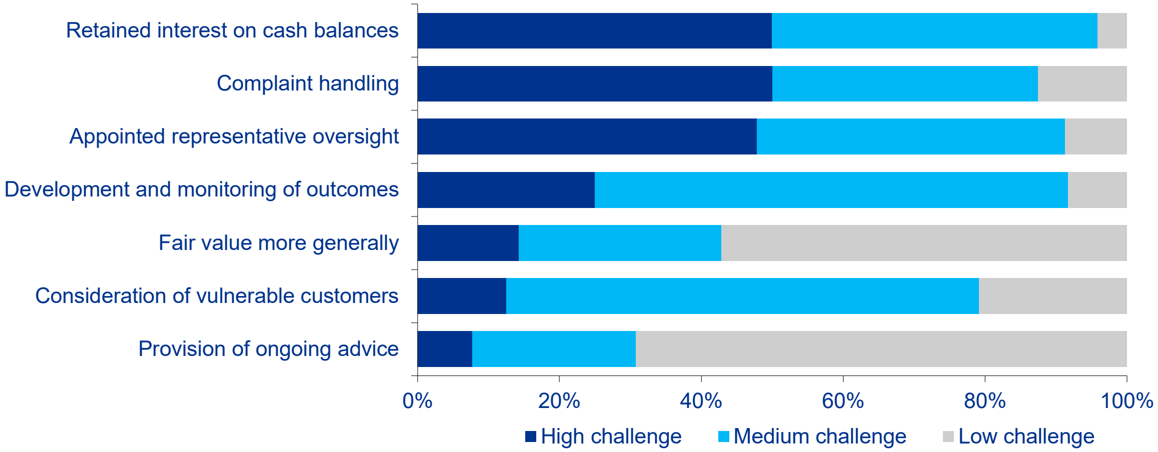
Trends in the data

- 77% of participants have implemented standalone consumer duty frameworks and operating models.
- 93% of participants reported that the first line of defence is responsible for performing fair value assessments. With first line product managers being responsible a majority of the time (64%).
- In terms of the four Consumer Duty outcomes, 70% of participants reported that price and value is a high priority upcoming focus area, followed by products and services (61%), consumer support (59%), and consumer understanding (43%).
- While there has been significant regulatory engagement with firms regarding the provision of ongoing advice, less than 10% of firms identified this as a significant challenge for their business. On the other hand, retained interest on cash balances (52%), complaint handling (48%), and Appointed Representative oversight (50%) are areas of significant challenge for participants.

Highest priority consumer duty outcomes participants expect to focus on over the next 12 months



Most challenging areas of FCA supervisory focus



KPMG View

The FCA is using all the tools at its disposal to engage proactively with firms across the industry to improve outcomes.

Meanwhile firms are working to embed the Duty into business-as-usual processes.

The results of the survey illustrate the longevity of certain challenges – such as around retained interest on cash balances.

On price and value specifically, it's noteworthy that this is expected to be the greatest focus area for firms over the next 12 months out of the four Consumer Duty outcomes.

Firms continue to join up the fair value assessment (FVA) process with wider product governance arrangements and work on ensuring that all statements can be substantiated with robust MI and evidence. They are also grappling with the challenging concept of assessing product-level profitability via activity-based costing. This also applies to fund managers – who have been subject to fair value requirements since 2019.

Further FCA publications and observations can be expected on Consumer Duty-related topics soon – including on ongoing advice, vulnerable customers, and consumer support. Firms can also expect further scrutiny of their complaints handling arrangements, platform transfer times, and interest retained on cash balances.

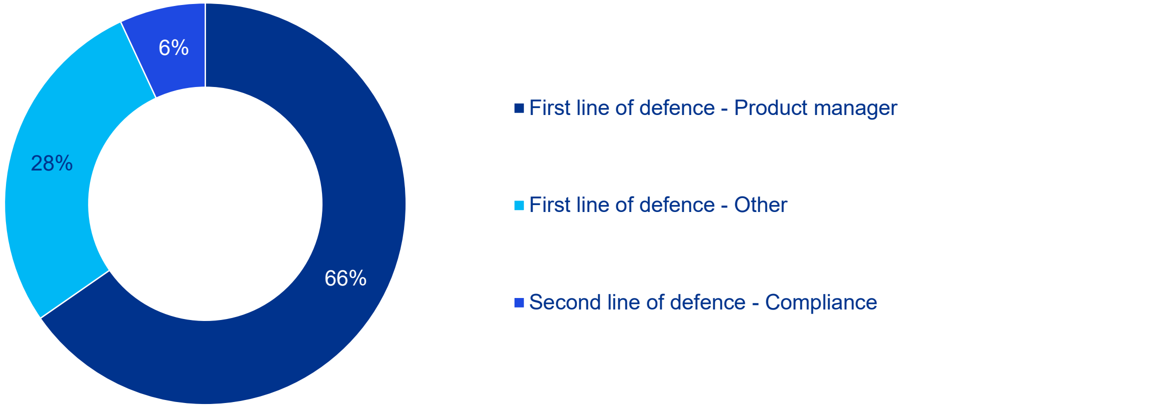
Consumer Duty

First line product owners are typically responsible for performing fair value assessments.

Trends in the data

- For over 90% of participants, the first line of defence is responsible for performing fair value assessments.
- For many firms, the product manager (or equivalent) is directly responsible for this assessment.
- Only 6% of firms reported that their compliance function was responsible for performing fair value assessments.

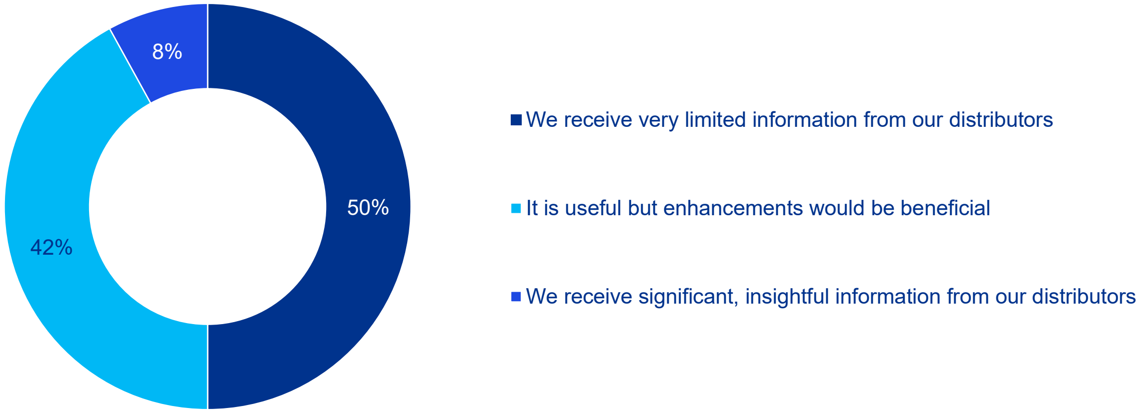
Role of individuals who are responsible for performing fair value assessments/assessments of value



Only 8% of firms reported that they receive high-quality information from their distributors, making fair value assessments – and wider product reviews – more challenging.

- 50% of firms stated that they only receive limited information from their distributors.
- 42% reported that they receive more complete data, but that enhancements would be beneficial.
- Only 8% of firms reported that they received significant and insightful information from their distributors.

Effectiveness of the Consumer Duty distributor to manufacturer feedback loop



KPMG View

One of the most practical challenges with implementing the Duty has centred around successfully transitioning implementation from the project phase to business as usual. In this context, some firms have overly-relied on the second line of defence.

The survey results are therefore reassuring in that they illustrate the first line defence is taking the lead on the fair value assessment process in the vast majority of participating firms.

However, the results also make clear that there is still significant room for improvement when it comes to the functioning of the distributor-manufacturer feedback loop.

While many had hoped that the introduction of the Duty would improve the flow of information between fund and portfolio managers and intermediaries, half of participants reported that they receive “very limited” feedback. And only a small minority receive insightful information. This picture is consistent with what we hear through our discussions with clients.

Despite the good foundations that trade bodies have laid via templates, further work is needed. In some cases – such as mass-market products that have a broad target market and may be distributed widely – further clarity from the regulator would be welcome.

More broadly, the impact on the Duty of the government’s pro-growth stance remains to be seen. However, we do not expect a ‘bonfire’ of regulation. To date, the FCA has only committed to removing the “board champion” role, ahead of a post-implementation review of the Duty. It will also ensure future consumer protection consultations consider whether existing requirements under the Duty suffice.

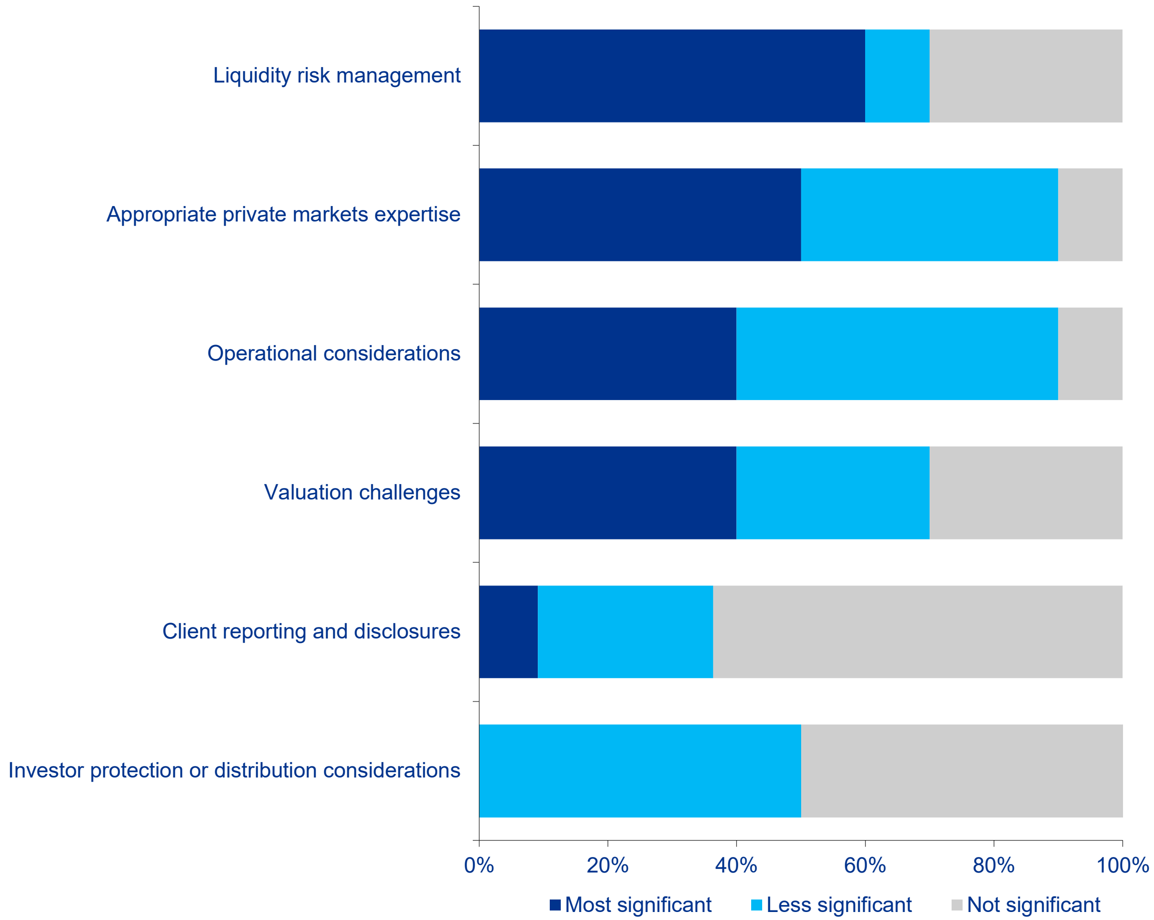
Private markets

Over half of the participants who plan on launching private asset funds intend to use either the LTAF or ELTIF structures to do so. However, no firms intend to launch a private asset-focused ETF or tokenised product in the near future.

Trends in the data

- 56% of firms who are launching new private asset funds expect to launch funds utilising either a Long-Term Asset Fund (LTAF) or a European Long-Term Investment Fund (ELTIF) structure. Interestingly, all firms who intend to adopt these new structures also intend to launch traditional funds in parallel.
- No participant expects to use an exchange-traded fund (ETF) or tokenised approach to launch a private asset fund over the next 12 months.
- 60% of participants highlight liquidity risk management as a key barrier to launching an LTAF or ELTIF. Appropriate private market expertise (50%), operational considerations (40%), and valuation challenges (40%) were also cited as significant barriers.
- Regarding valuation challenges, only 26% of participants have adjusted their approach to asset valuation governance and oversight as a result of the FCA's review that was launched in 2024.

Most significant barriers to an effective LTAF or ELTIF launch?



KPMG View

Regulators have been making new vehicles available and adjusting existing structures to promote the democratisation of private assets to retail investors.

After a slow start to the UK's LTAF regime that was launched in 2021, fund launches are beginning to accelerate – with a variety of managers (including host authorised fund managers) bringing products to market across a variety of asset classes.

Similarly in the EU, the ELTIF 2.0 package – finalised in 2024 – has made the product more attractive to managers and already led to a significant increase in the uptake of the product.

However, launching such products is no easy feat – as the survey results show. Firms need to bring together private markets expertise alongside experience managing open-ended funds. And meet the specific challenges associated with launching these novel vehicles.

The survey results are interesting in this respect, showing that careful thought needs to be given to liquidity management and operational considerations – while ensuring sufficient expertise is in place. Valuation is also an ongoing challenge for firms, particularly as they need to move beyond the traditional quarterly approach to daily valuation in some cases. In all cases, a consistent operating model can help fund managers navigate these challenges.

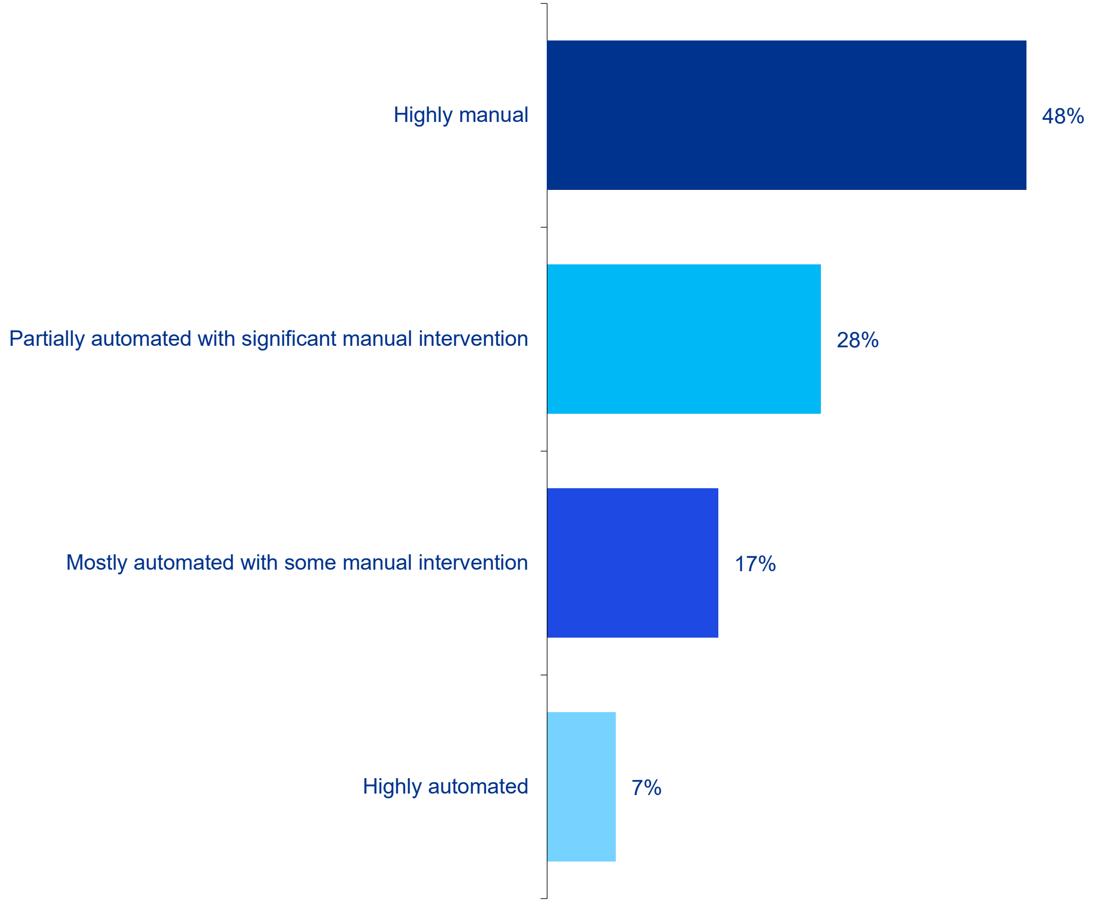
Digitalising the approach to regulatory change

Leading firms are deploying automated tools to streamline their regulatory change programmes, potentially reducing the specialist FTE required across their business and reducing the risk of non-compliance.

Trends in the data

- With many firms highlighting the need for specialist skillsets, leading firms are working to deploy more automated solutions.
- 48% of firms have highly manual approaches to regulatory driven change management, which we see correlating with increased overall headcount within their Risk and Compliance functions compared to peers.
- Just over half of participants have deployed systems to help automate regulatory change to varying extents. Introducing automation has the potential to enable a more efficient operating model.

Participant approach to regulatory driven change management



KPMG View

The ongoing high volume of new regulatory requirements and divergence across jurisdictions requires risk and compliance functions to dedicate significant resources to change management initiatives.

The FCA has flagged the importance of getting this right. In its 2024 letter to asset managers on its supervisory priorities, it noted the importance of effective regulatory change management.

However, many firms are still operating highly manual processes.

With leading firms deploying automated tools and techniques to ensure clear traceability from new rules to corresponding changes to policies, procedures and controls, we are observing a split across the industry.

Leading firms are combining regulatory and strategic change, underpinned by technology. They are starting to see the benefits from early investments in automation, while other firms are still operating in a highly manual way. We expect that this gap will close as automated solutions become more accessible and as barriers for entry lower.

However, until then, firms without more automated processes will be at a disadvantage. They will potentially require more resources to deliver the same tasks and projects, and delivery timelines may also be impacted.

03

Capital and liquidity requirements

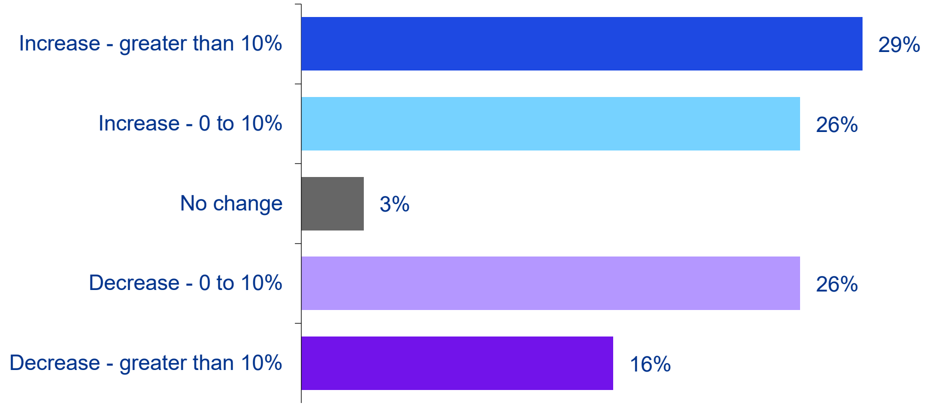
Changes in capital and liquidity requirements in 2024

Requirements for the largest firms have increased in the last 12 months, with nearly half of these being subject to an FCA add-on.

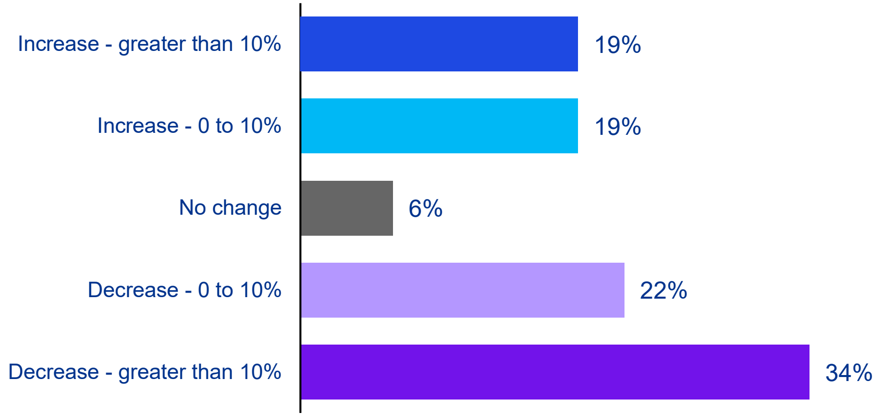
Trends in the data

- For 55% of firms, capital requirements have increased between 2023 and 2024. Where capital requirements have increased, the most significant driver was due to higher ongoing harm assessment requirements (47%). Individual Capital Guidance (“ICG”) issued by the FCA drove increases for 35% of firms, with the remaining 18% of increases being driven by wind-down requirements.
- Increases were most likely amongst the largest firms (in the P1 category) where 70% had higher capital requirements.
- Smaller firms (in the P3 category) have assessed year-on-year reductions in capital requirements, with 67% of P3 firms now have lower capital requirements. This is largely driven by falls to both their ongoing harm assessment and their wind-down requirements.
- For liquidity, only 34% of firms saw increases in requirements. Where increases occurred, the driver of this was split evenly across the ongoing harm assessment, Wind-Down Planning, and Individual Liquidity Guidance (“ILG”) issued by the FCA.

Change in capital requirements for firms between 2023 and 2024



Change in liquidity requirements for firms between 2023 and 2024



KPMG View

Increases in capital requirements based on firm self-assessments through the ICARA process suggest that growth in the size of market participants has led to associated growth in capital requirements. When we look at the largest firms in the survey (in the P1 category), most of these firms have identified increases. In our view, this likely reflects that the past 12 to 18 months have seen continued growth in the size (AUM) and activities of the largest wealth and investment management firms, with a corresponding increase in the capital held as a result.

On the other hand, with liquidity there is trend where significant reductions in regulatory requirements have occurred. For many firms, these decreases have arisen due to changes in their approach for assessing their wind-down liquidity requirement. This follows on from the FCA’s IFPR observations reviews in 2023 which set explicit expectations for firms to perform a full cashflow analysis throughout the wind-down period. In our experience, as part of this exercise, many firms have reassessed key wind-down assumptions and the impact of liquidating their balance sheet in response. For some, this leads to reduced liquidity requirements due to lower net cash outflows in wind-down.

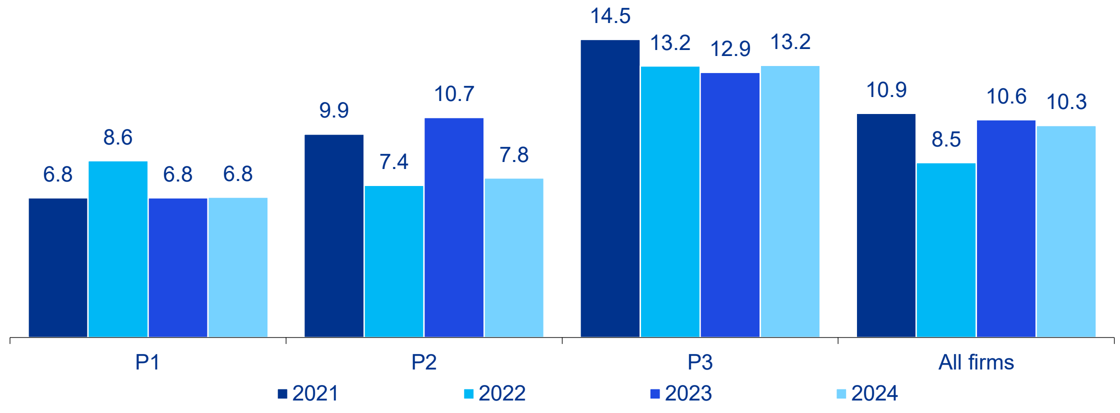
Overall capital requirements

There is a continuing trend of stability in capital requirements proportional to AUM/A. For some, this metric has significantly reduced due to higher AUM/A.

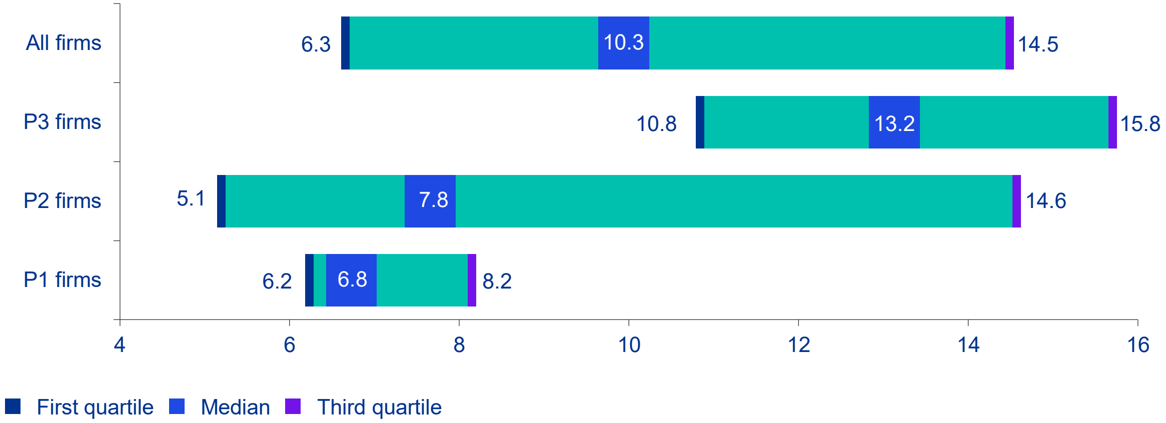
Trends in the data

- The median capital requirement for the largest, P1, firms remained static at 6.8bps of AUM/A. Therefore, while the absolute requirements for many of these firms have increased, proportionally the impact of this has been offset by growth in AUM/A.
- Similar trends exist for P3 firms, where proportional requirements increased slightly to 13.2bps (2023: 12.9bps). Requirements for P2 firms have decreased, from 10.7bps in 2023 to 7.8bps in 2024.
- Vertically integrated wealth and asset management firms typically had the highest proportional requirements. Investment platforms and administrators also have proportionally higher requirements compared to other participants.
- Large asset managers (firms with over £200bn in AUM) had significantly lower proportional requirements, with many of these firms reporting proportional requirements less than 4bps.

Median overall capital requirements as a proportion of AUM/A (in basis points)



Distribution of overall capital requirements as a proportion of AUM/A (in basis points)



KPMG View

The prudential regime for investment firms has now been in force for three years and, in our view, this has now led to capital requirements for many wealth and asset managers stabilising. Firms have now been through multiple ICARA and WDP assessment processes and the FCA has completed their supervisory reviews of the largest firms (which we analyse the results of later in this report).

There continues to be a broad range of proportional requirements across firms, with significant variances between firms who have similar business models being reflected in the distribution of capital requirements. These differences may be due to firm specific idiosyncrasies (e.g. large contractual exit costs leading to very large wind-down requirements) or due to significant prudence adopted in key subjective judgement areas in self-assessments.

Where firms hold significantly more capital than peers for the same risks, in our view it is likely that they will begin to reassess their approach to the ICARA and WDP to ensure that they are not being overly conservative compared to peers.

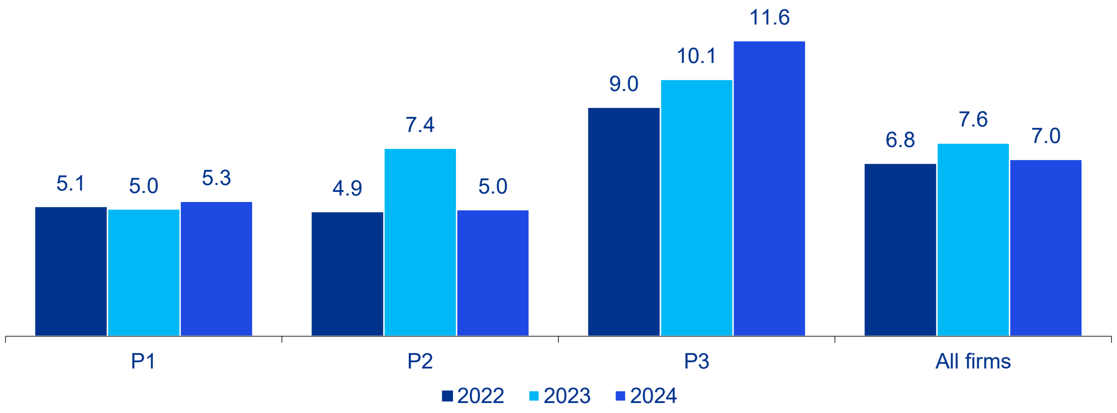
Overall liquidity requirements

While many small firms had year-on-year reductions in their liquidity requirements, proportionally these have increased relative to AUM/A.

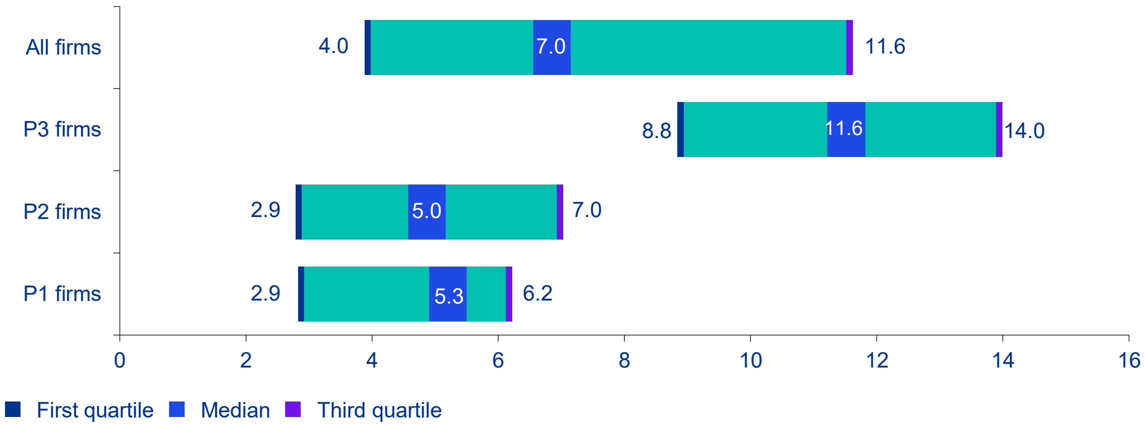
Trends in the data

- Across all firms, the median overall liquidity requirement is 7.0 bps of AUM/A, which has slightly decreased from the previous year (2023: 7.6bps).
- For larger, P1, firms there was a small increase in proportional liquidity requirements from 5.0bps in 2023 to 5.3bps. The smallest, P3, firms had a more significant increase in proportional requirements from 10.1 bps to 11.6 bps.

Median overall liquidity requirements as a proportion of AUM/A (in basis points)



Distribution of overall liquidity requirements as a proportion of AUM/A (in basis points)



KPMG View

Liquidity requirements were new to all firms when the IFPR came into force three years ago and there continues to be significant focus from both firms and the FCA on liquidity assessments.

Where firms do not trade on own account, assessing the amount of liquidity needed on an ongoing basis is typically performed through liquidity stress scenarios which leverage other parts of the ICARA (e.g. operational risk assessments) and also consider key liquidity specific risks (e.g. for funding client money shortfalls). This approach is usually appropriate due to their underlying liquidity risk profile and the structure of cashflows for wealth and asset managers. However, in our experience there can be considerable differences in the methodologies firms use for these assessments. Leading firms clearly articulate their liquidity risk profile and use methodologies which are underpinned by robust scenarios and back testing.

For liquidity in wind-down, in our experience the most significant area of focus from the FCA is on those firms that have not performed sufficiently detailed wind-down cashflow analysis or have adopted overly optimistic assumptions. As a result, many firms are reassessing their approach to liquidity in wind-down to ensure it is aligned with FCA expectations.

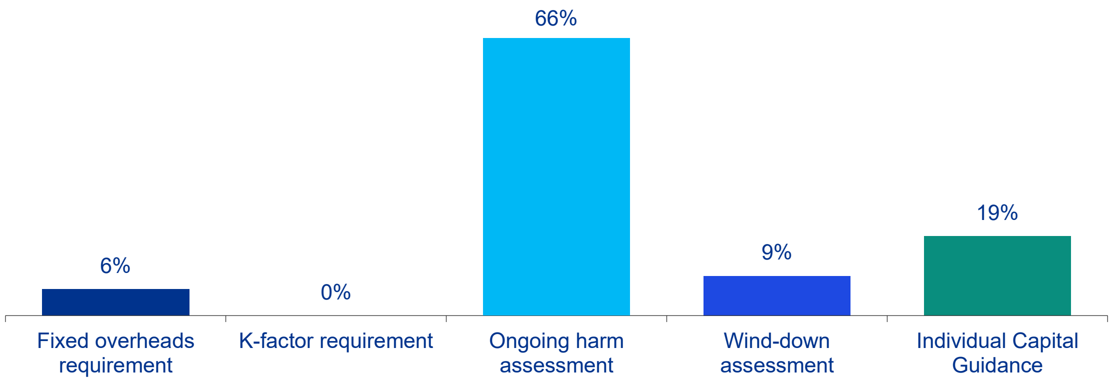
Drivers of capital and liquidity requirements

The ongoing harm assessment continues to drive capital requirements for most firms. For an increasing number, their requirements are also driven by the FCA's own assessment.

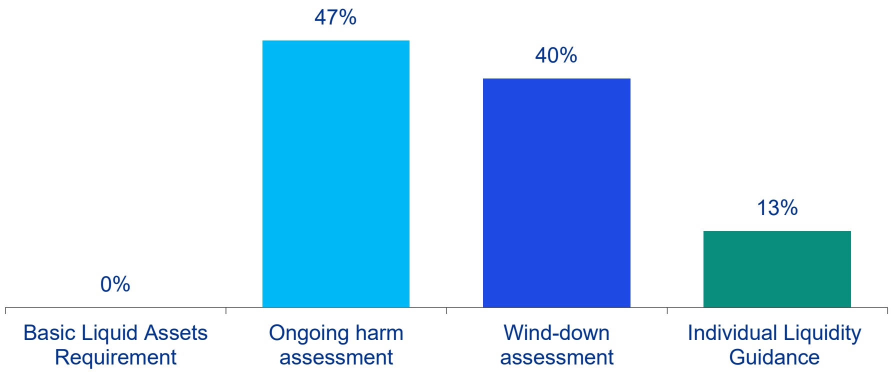
Trends in the data

- For capital, on a median basis, the ongoing harm assessment is 40% higher than the wind-down assessment across all survey participants.
- For liquidity, there is a much more even split between requirements for ongoing harm and requirements for wind-down.
- An increasing number of firms are subject to ICGs and ILGs set by the FCA; for 19% of firms, this drives their capital requirement (2023: 12%) and for 13% it drives their liquidity requirement (2023: 6%). These requirements were all set under the new regime now that all firms in the survey have transitioned away from legacy ICGs set under previous rules.

Overall capital requirements: driver of the capital requirement for each firm



Overall liquidity requirements: driver of the liquidity requirement for each firm



KPMG View

Under the IFPR, rules-based requirements act as floors to the self-assessments performed by firms. As firms typically self-assess add-ons above regulatory requirements, it is to be expected that these self-assessments are the most common driver of capital and liquidity requirements.

Given the operational risk profile of most survey participants, ongoing harm assessments are always most likely to be a key driver of their capital requirements. Now that the FCA has concluded their first round of supervisory reviews under the IFPR, there has been a small increase in the number of firms where regulatory driven capital requirements are the binding constraint and we analyse the reasons for this later in the report. However, we expect this to be a continued area of FCA focus given their publication in 2023 of guidance on the approach to the ICARA and WDPs.

Continuing a trend of last year, wind-down liquidity requirements are a significant theme coming through in firm assessments. In our experience, where firms have gaps and weaknesses in these assessments it typically leads to the FCA setting additional liquidity requirements during supervisory reviews and issuing them with actions to remediate gaps and weaknesses in their wind-down plan.

04 The ICARA

Governance and approach to the ICARA

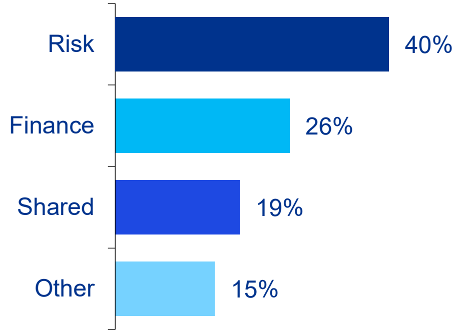
Both the ICARA and WDP assessments are most likely to be led by Risk and Finance respectively.

Trends in the data

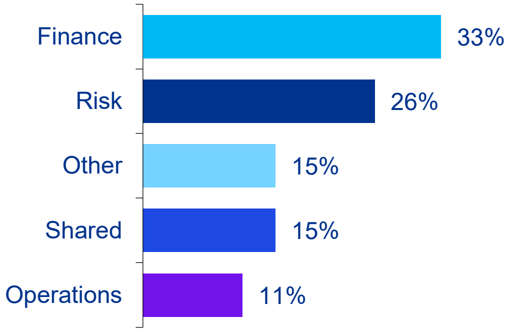
- For the ICARA, Risk (41%) and Finance (26%) are the most common owners of the ICARA document. 19% of participants adopt a hybrid approach of shared ownership between these two functions.
- For WDPs, Finance (33%) and Risk (26%) are the most common owners of the document. However, unlike the ICARA, there is a trend where some firms have owners in operations (11%) or other functions (15%).
- Where participants are part of a Group, 27% have been told by the FCA to perform a consolidated ICARA process.
- Most of Groups (42%) allocate capital requirements to entities using a metric-based approach (where key business metrics, such as AUM or headcount, are used to allocate capital to underlying entities). 29% use a scenario-based approach, where specific scenarios are defined for each relevant entity and capital is calculated in a bottom-up process. The reminder adopt a hybrid approach using both methods.

Functional ownership of key capital and liquidity assessments based on SMF responsibilities

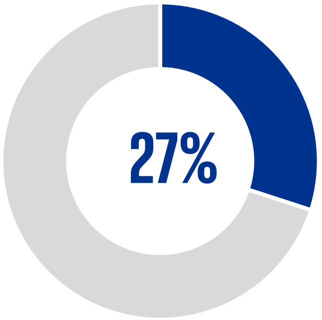
ICARA document



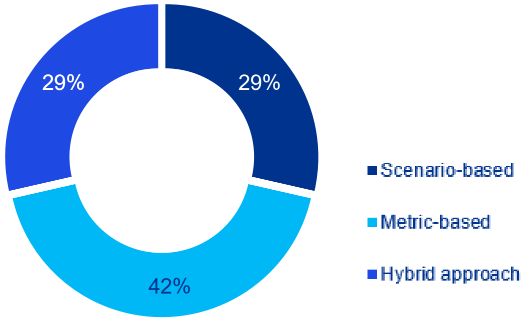
Wind Down Plan document



Percentage of firms performing a consolidated ICARA due to an FCA request



Approach for allocating capital requirements across Groups



KPMG View

At its core, the ICARA document assesses key risks in a business, and it is no surprise that these are typically owned by Risk functions. As the ICARA requires significant input from Finance, we are seeing an emerging trend of shared ownership, where Risk own key risk assessment components and Finance own key financial information and assessments. Usually this also involves the Risk function identifying the top risks faced by the business and Finance quantifying key parts of the ICARA (e.g. business plan stress testing).

The FCA's focus on WDPs in recent years has been on operability and this is likely a key contributor to the ownership of some Wind-Down Plans sitting with Operations. In our experience, a robust Wind-Down Plan requires significant input from right across the business and many firms experience benefits from having these parts of the plan being 'business led'. However, given the impact of WDPs on both the Risk Management Framework and capital/liquidity assessments, there will always be inputs from Risk and Finance respectively.

KPMG

Capital requirement assessments in the ICARA

Operational risk is the most significant component of risk assessments in the ICARA.

Trends in the data

- All firms hold capital for operational risk in the ICARA and this forms most of the requirement (83%) identified by firms.
- Many firms also self-assess capital add-ons for credit and market risk, however, amounts held for these risks (8% and 5% respectively) are significant less than operational risk.
- 30% of firms hold capital for 'other' risk types outside of these key risk categories. The most common 'other' risk is business and strategic risk (where 16% of firms hold capital for these risks). Typically, this formed 4% of their overall capital requirement.

Percentage of firms holding capital for harm arising from the following risk types

100% Operational risk

87% Credit risk

73% Market risk

30% Other risks

Median percentage of capital held for each risk type as part of the harm assessment

KPMG View

Given the maturity of the capital assessment methodologies being used by participants, we would expect operational, credit and market risk assessments to continue to be key parts of the ICARA. Many firms will now be confident in their approach to these capital assessments and are unlikely to make significant changes in the future.

However, in our experience the FCA can and does still challenge firms on underlying methodologies, particularly where capital held for key risks makes the firm an outlier to peers or where capital assessment methodologies are highly complex and not fully understood in the firm itself.

In our experience, the FCA does usually accept a broad range of approaches to capital assessments in the ICARA, however these need to be underpinned by robust governance and validated underlying methodologies.

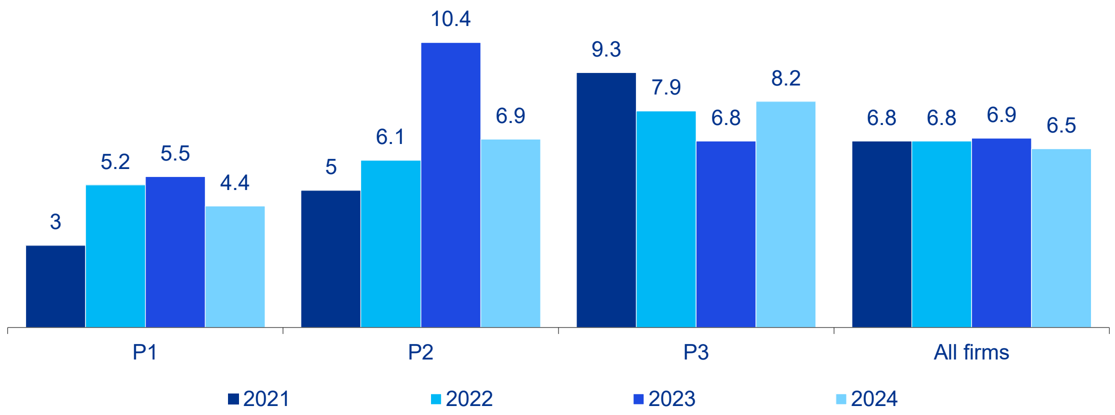
Operational risk capital requirements

Proportional operational risk requirements for many firms have decreased year-on-year, however, this is driven by changes in AUM/A.

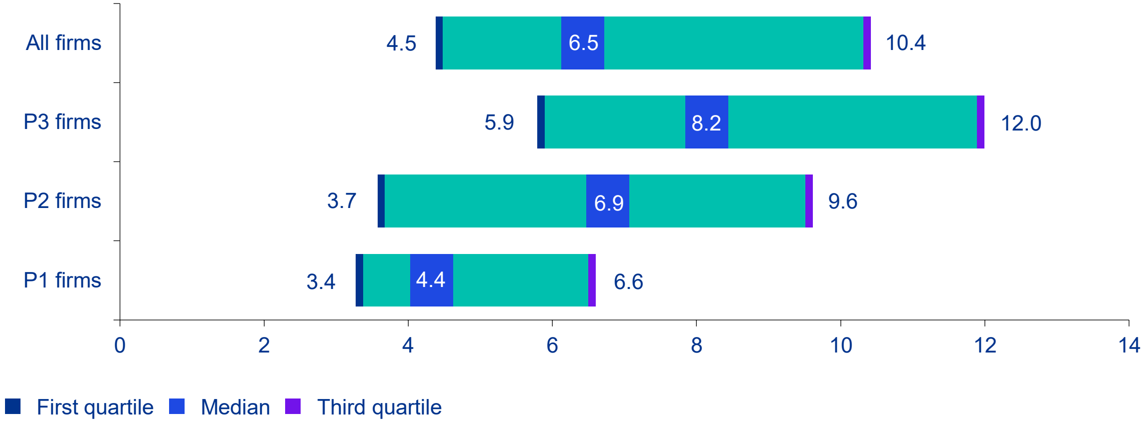
Trends in the data

- Proportionally, P1 firms hold 4.4bps of capital as a proportion of AUM/A for operational risk. This is lower than in 2023 but reflects growth in AUM/A for the largest firms.
- P2 firms hold 6.9bps (2023: 10.4bps) and P3 firms 8.2bps (2023: 8.2 bps). For P2 firms this represents a significant year-on-year decrease. However, further analysis shows that this increase is driven by changes in the survey participants in this category, as opposed to year-on-year decreases across firms.
- Across all firms, the median amount of capital held as a proportion of AUM/A for operational risk is 6.5 bps (2023: 6.9 bps) and we continue to see significant dispersion between firms in terms of amounts held.

Median operational risk requirements as a proportion of AUM/A (in basis points)



Distribution of operational risk requirements as a proportion of AUM/A (in basis points)



KPMG View

Typically, as a firm's AUM/A increases, its operational risk assessment in the ICARA also increases. However, this is not a linear relationship, with larger firms benefiting from apparent economies of scale through proportionally lower capital requirements.

There are, of course, a broad range of factors that impact operational risk assessments. Different business operating models and products will create a different operational risk profile.

In our experience, firms that capture more of the value chain, such as vertically integrated wealth managers with their own funds and investment platform, have significantly larger proportional capital requirements compared to others. Likewise, where an asset manager has a more complex product offering and footprint than a peer, this is likely to also lead to higher requirements.

In our experience, leading firms are starting to assess the ways to reduce their risk profile (for example through legal entity rationalisation or changing operating models) and to decrease capital requirements as a result.

Approaches to operational risk assessments

Firms are most focussed on execution and process issues in their operational risk scenarios. Many continue to use a statistical model in their assessments and benefit from a 32% reduction in capital requirements as a result.

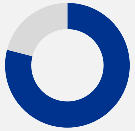
Trends in the data

- On a median basis, survey participants are modelling more operational risk scenarios across several of the Basel operational risk categories compared to previous years. In 2024, participants modelled a median of 12 operational risk scenarios, compared to 9 in 2023.
- Where firms use a statistical model, 79% assume some form of diversification benefit (i.e. assuming that not all scenarios will occur in the same time period). Where firms use diversification, the median reduction in capital requirements is 32% (2023: 32%).
- 13% of firms reduce their capital requirements by using insurance as a mitigant for operational risk. Where firms use insurance, the median reduction in capital requirements is 17% (2023: 7%).

Median number of operational risk scenarios by Basel operational risk category

Execution, delivery and process management	4
Clients, products and business practices	2
Business disruption and system failures	2
Employment practices and workplace safety	1
External fraud	1
Internal fraud	1
Damage to physical assets	1

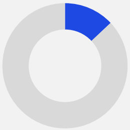
Diversification benefit use in assessments using a model



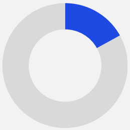
79%
Firms using operational risk diversification in a statistical model

32%
Median capital reduction applied in a statistical model through diversification

Insurance mitigation use in all assessments



13%
Firms using insurance mitigation



17%
Median capital reduction applied through insurance mitigation

KPMG View

Historically, investment firms have either used simple approaches to operational risk quantification based on performing scenario analysis or quantified requirements using a statistical model. Typically, larger firms will use statistical models given their size and complexity will usually allow them to have specialists in the Risk function to maintain and run such models. Even where statistical models are used, these still require significant levels of expert judgement and input from risk owners.

While using a statistical model may result in a more robust approach, several firms subject to supervisory reviews have been challenged on their use by the FCA. This includes instances where model governance and validation frameworks were not in place and examples of key personnel not demonstrating a sufficient understanding of models used.

Regardless of approach, there is continued FCA scrutiny on firms being able to demonstrate operational risk assessments are used in the Risk Management Framework. For example, embedding control assessments into the process to understand key controls and weaknesses in these or linking the assessments to other risk processes, such as operational resilience.

KPMG

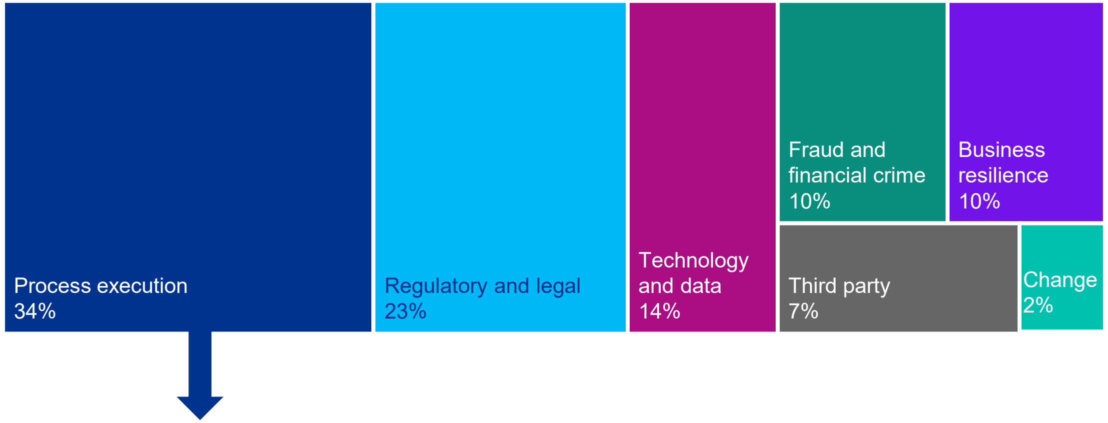
Risk coverage and capitalisation in operational risk assessments

Firms hold the most capital for risks linked to process execution and regulatory and legal risks. This shows that, while coverage across risk categories can be broad in terms of individual scenarios, capital held is focussed on key risks.

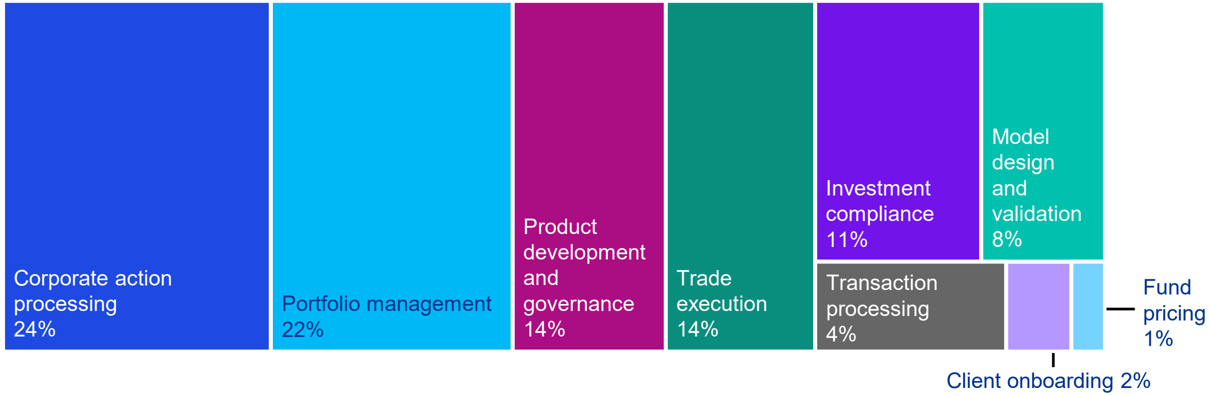
Trends in the data

- 90% of firms hold capital for Process execution risk scenarios, typically representing 34% of their overall operational risk capital requirement.
- Firms also hold capital for the following risk categories; Regulatory and legal (90% of firms), Fraud and financial crime (87%), Third party (80%), and Technology and data (80%).
- Very few firms hold capital for business change risks (10%) and fewer still hold capital for people risks (5%). Where investment managers do hold capital for these risks, they typically represent a small proportion of their overall operational risk capital requirements (2% for business change risks and less than 1% for people risks)
- Focussing on process execution, risks around corporate action processing (24%) and portfolio management (22%) form a significant proportion of overall capital requirements. Trade execution scenarios were by far the most common, but typically only represented 14% of the overall operational risk capital requirement.

Typical proportion of capital held for each key operational risk category



Typical proportion of capital held for process execution risks



KPMG View

A common challenge faced by all firms is determining which operational risks to capitalise for and how much capital should be held for these risks. For the first time in our survey, we have analysed the types of scenarios modelled (using our own risk taxonomy categories) and how much capital this results in them holding.

The focus of these assessments on both process execution and regulatory/legal risks reflects the agency nature of wealth and asset management firms, as well as the significant regulatory change and associated risks the sector has been through in the past 10 years.

As firms continue to adopt more advanced technologies across their business, increase their reliance on third party service providers and the FCA focusses on operational resilience, we expect more capital will be held for risks associated with these activities.

Leading firms are also increasingly using this analysis to focus on managing risks in the business where the most capital is held. While the inherent risk of process execution or regulatory/legal risks may be well understood already, improvements in controls and reductions in capital held can provide a business case for implementing risk reduction measures,

Approaches to corporate liquidity risk assessments

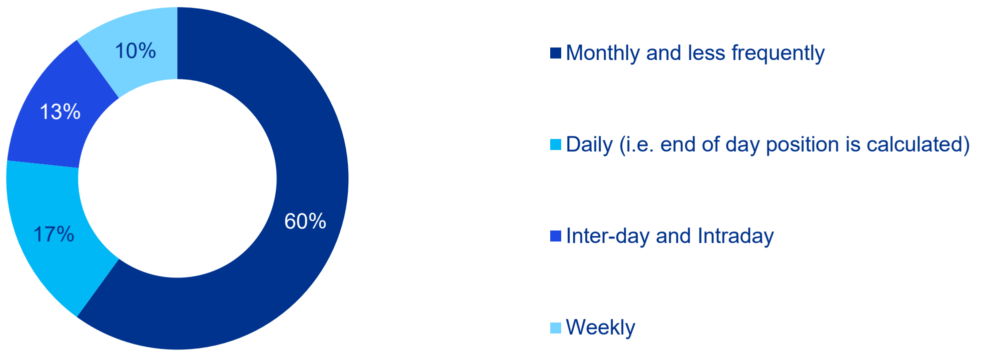
For many firms, liquidity requirements are driven by medium term negative cashflows in stress test scenarios. The approach to performing liquidity stress testing using monthly cash flow analysis likely reflects that many survey participants are not exposed to material intra-day liquidity risk.

Trends in the data

- 50% of participants do not model a liquidity stress tests which leads to their firm having net negative cash flows. Where negative net cash flows are identified, 38% of firms expected to have negative cashflows for longer than 6 months.
- In recent publications, the FCA has stated that some firms should consider modelling granular liquidity assessments. However, of the firms surveyed, only 40% model liquidity stress tests that go beyond monthly analysis.

Length of time firms forecast negative net cashflows as part of their liquidity stress testing exercise

Granularity levels of modelling considered for liquidity stress testing



KPMG View

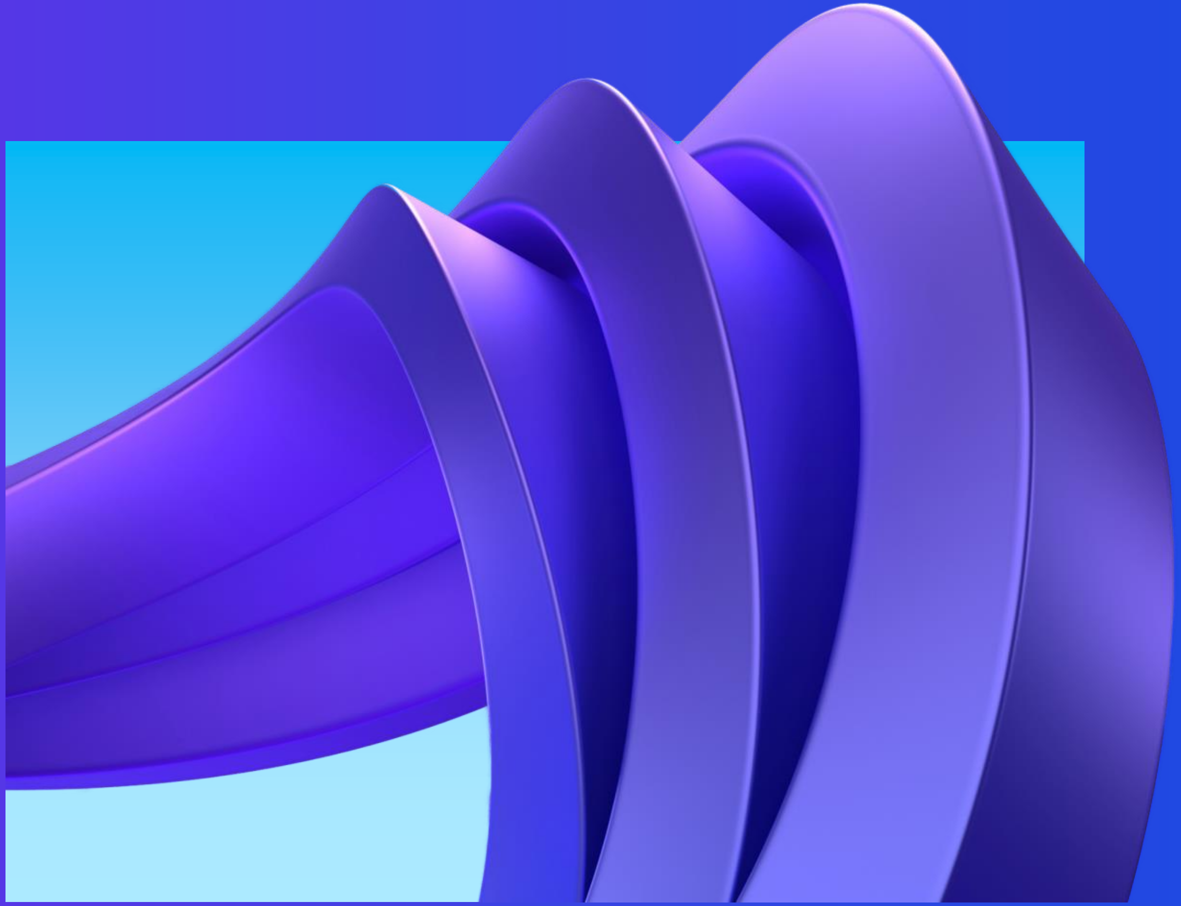
Due to the cash generative nature of wealth and asset management businesses, there has historically been limited focus from firms themselves on liquidity risk. However, since the introduction of the IFPR the FCA has reiterated that while a firm's liquidity profile may be simple, it does not mean it is free from liquidity risk.

In our experience, firms who do not assess any cash outflows in liquidity stress testing are likely to be challenged by the FCA on whether stresses performed are "severe but plausible" or if they are assessing liquidity risks over an appropriate time horizon. This is especially pertinent given some operational risks, such as process execution errors, are also likely to have a liquidity impact over the short-term.

Therefore, for robust liquidity stress testing leading firms consider both short-term liquidity needs (e.g. considering inter-day stress scenarios) and longer-term liquidity issues. The most severe of these is then used to determine the liquidity requirement.

05

Wind-down plans



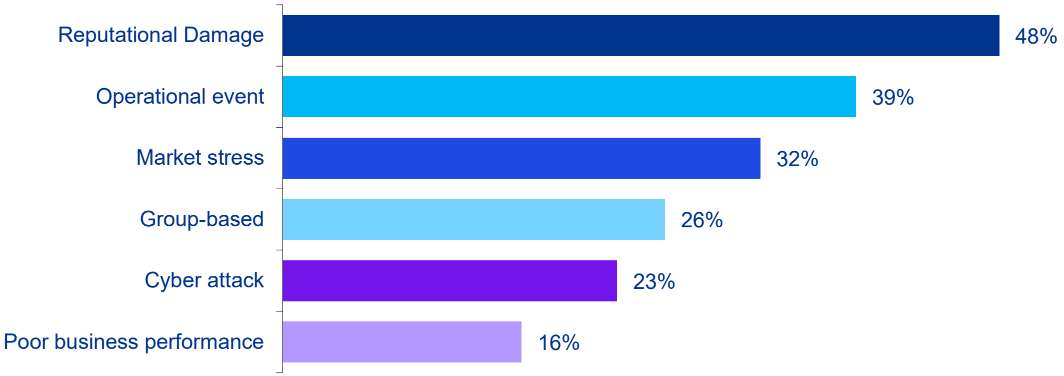
Approach to Wind-Down Planning

Wind-down scenarios typically include a broad range of risks given these scenarios are designed to break the business. Strategies to wind-down continue to be split between those firms that assume full termination of client accounts and those that assume a client transfer would be possible.

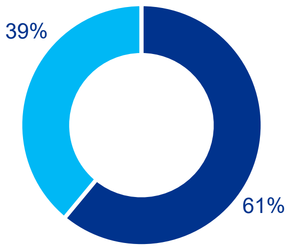
Trends in the data

- 68% of participants assume a combined scenario occurs, where several distinct risk events occur which then results in wind-down.
- In terms of scenario components, 48% of participants assume some level of reputational damage occurs and results in the need to wind-down. 39% of firms assume an operational event is a factor leading to the need to wind-down.
- Firms in groups are divided in their approach to Wind-Down Plans ("WDPs"). 38% of participants develop a full WDP for each MIFIDPRU firm and also their group as a whole. However, the majority (56%) produce a single WDP on a group basis with entity-level consideration throughout.

Most common risk events used in wind-down scenarios

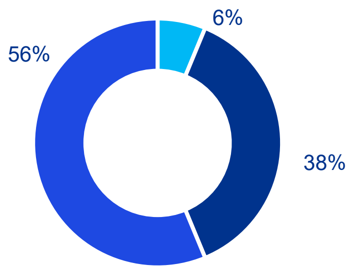


Wind-Down strategy approaches



- Full liquidation/termination of client relationships
- Transfer/sale of a book of business but for a notional amount (i.e. sale value is £1)

Approach to WDPs in groups



- Single group focused plan
- Full plans for each in-scope entity
- Single group-level plan with entity level detail throughout

KPMG View

One of the consistent challenges faced when creating a WDP is defining a scenario that is severe enough to cause the business model to become unviable while still being tied to a realistic event. This can also be challenging in profitable businesses, For example, in our experience, AUM/A must fall by over 50% before some firms become loss making.

Where a wind-down scenario is overly abstract or unrealistic, it can be challenging to get buy-in to the WDP development process from across the business. This can then lead to a less detailed WDP and one that is more likely to be challenged by the regulator.

A core assumption in WDPs and area of much debate amongst firms is whether they can assume part, or all the business is transferred in wind-down. In our experience, the FCA will accept firms assuming transfers to third party providers occur during a wind-down period. However, this needs to be supported by robust operational analysis of the steps required to complete a transfer, the resources needed to support this and conservative assumptions around the associated timelines.

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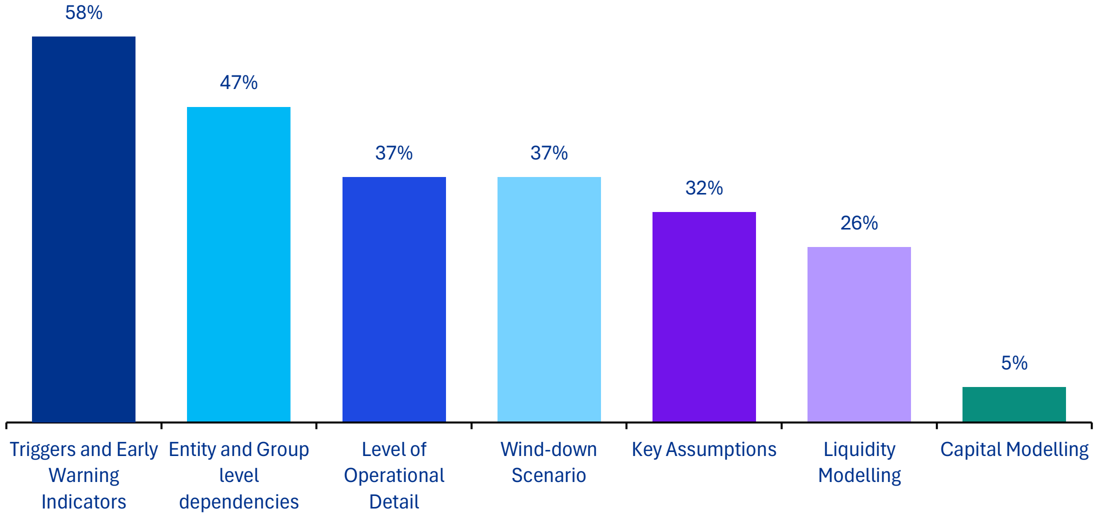
Operational analysis within the Wind-Down Plan

The FCA has issued granular guidance on their expectations for WDP documents. There is significant focus on having 'operable' plans and firms continue to fall short in demonstrating operability.

Trends in the data

- Where participant WDPs have been reviewed by the FCA, the most common area of feedback was on the triggers and early warning indicators (58%) defined by firms. Group risk and the identification of intragroup dependencies (47%) has also been a key area of FCA focus.
- Around 25% of participants have take actions to change their business due to WDP assessments. For example, 10% of firms have sought to renegotiate key contracts due to exit fees.

Most common area of feedback identified by the FCA in Wind-Down Plans



Most common changes and business improvements made due to Wind-Down Planning

10% Renegotiation of key contracts and exit fees

10% Review of intra-group agreements

5% Put in place wind-down specific MI

KPMG View

The FCA has stated that they "expect all WDPs to be credible, operable and to minimise harm".

In our experience, for a plan to be credible, the key assumptions must be suitably conservative, and the plan must be built on a stressed backdrop (to reflect that wind-down is likely to occur when both a firm and the market is under financial stress).

For operability, we typically observe the FCA assess whether the plan is designed is a way that means it can be implemented in practice. For example, assessing if the wind-down indicators have calibrated based on the outputs reverse stress tests. In an extreme scenario, the FCA would need to oversee a wind-down. Therefore, the plan typically requires enough operational detail to enable an external reader to understand what steps need to be taken and when to wind-down in an orderly manner.

Finally, throughout the plan there is an expectation that it appropriately identifies harms to key stakeholders (clients, the market) and outlines appropriate actions to mitigate these.

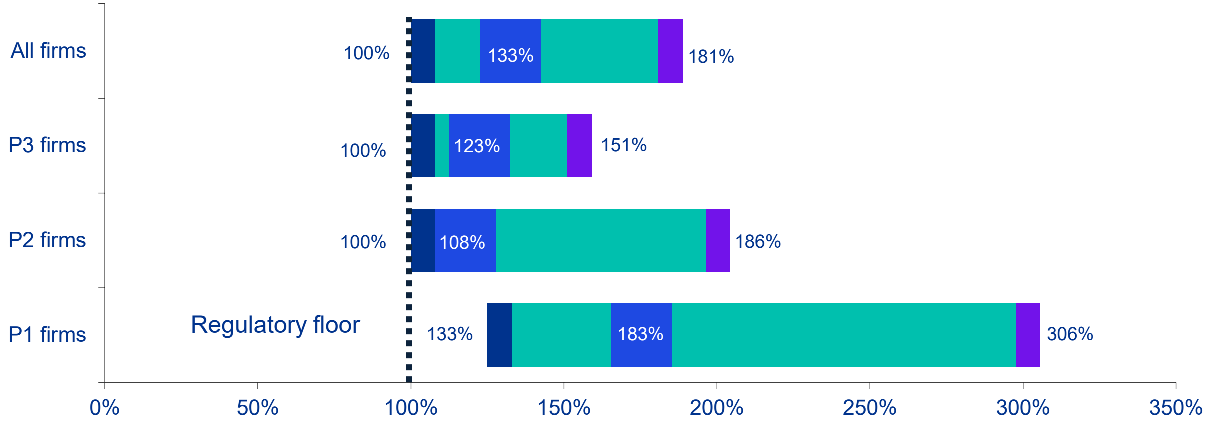
Wind-down financial resource assessments

Compared to ongoing operating costs, the wind-down capital and liquidity requirements for larger firms are typically higher than for smaller firms.

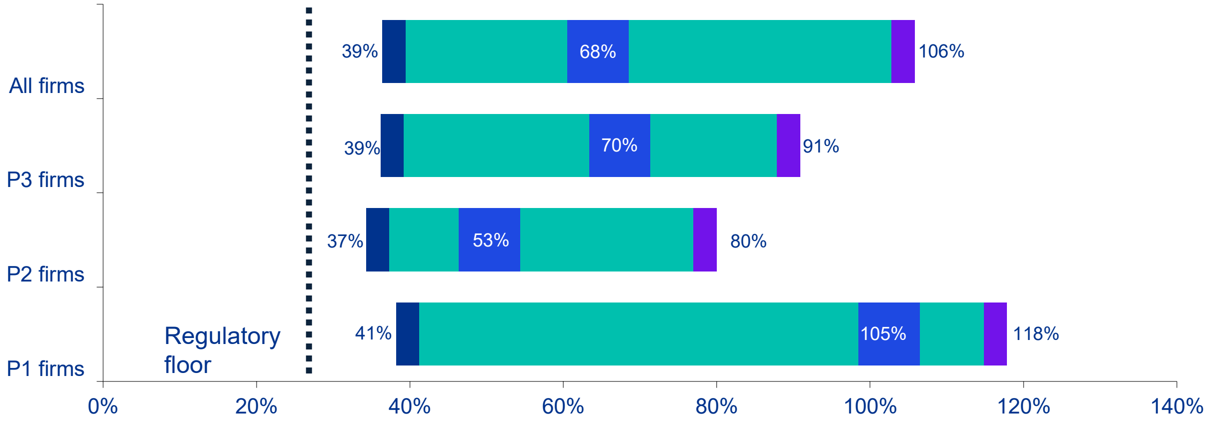
Trends in the data

- Comparing wind-down capital requirements to the Fixed Overheads Requirement (“FOR”), for firms the median cost of wind-down is 183% (2022: 177%) of the FOR. For smaller firms, this figure is 123% (2022: 131%).
- For over 25% of firms, wind-down capital requirements are set at the regulatory floor (i.e. the Fixed Overheads Requirement).
- For liquidity requirements, there is a trend of larger firms also having proportionally higher wind-down requirements. However, fewer firms assess their wind-down requirement for liquidity to be limited by the regulatory floor.
- For both capital and liquidity requirements, there is significant variance in proportional requirements.
- For liquidity, the cashflow modelling performed by firms for wind-down typically considers monthly cashflows (73%). 14% of firms perform daily cashflow analysis as part of their Wind-Down Plan modelling.

Distribution of wind-down capital requirement as a proportion of the FOR



Distribution of wind-down liquidity requirement as a proportion of the FOR



KPMG View

A key output of WDPs is the amount of capital and liquidity required to wind-down in an orderly manner.

In our experience, there is significant FCA scrutiny on the liquidity required to wind-down a business and we have observed some industry participants identify very significant liquidity requirements from wind-down exercises. For large firms, which have been subject to more recent FCA SREPs, it is common for wind-down liquidity requirements to be significantly larger than the Fixed Overheads Requirement.

Many firms usually expect to be cash negative throughout most of the wind-down period and have identified significant additional wind-down specific costs (i.e. retention payments, termination fees, and lease costs).

Firms that have not been subject to a SREP since the implementation of the IFPR have proportionally lower wind-down requirements. This may indicate that their approach to the financial resource assessment may not meet FCA expectations.

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The SREP 06

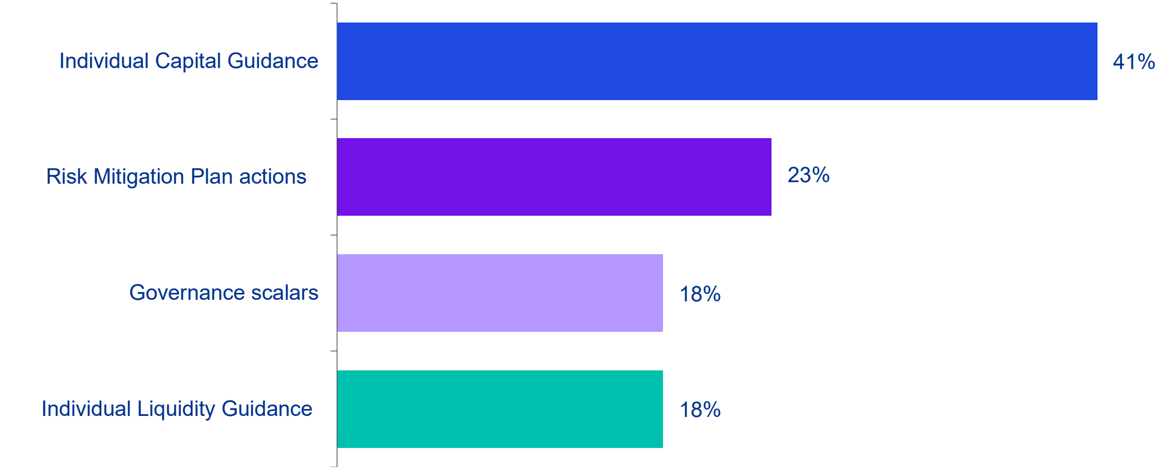
Outcomes of recent FCA SREPs

Most survey participants have been subject to an FCA supervisory review in the past three years. Of these firms, 41% were issued with additional capital or liquidity requirements.

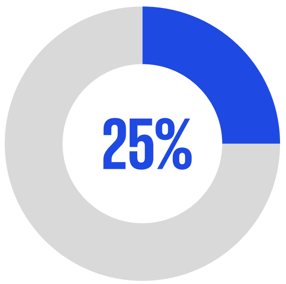
Trends in the data

- The FCA has completed their initial set of supervisory reviews under the IFPR. 41% of firms subject to these reviews were issues with ICGs (2023: 33%), suggesting that the likelihood of being issued an ICG increased during the review period.
- There has been an increase in the number of firms receiving Risk Mitigation Plan actions to 23% (2023: 7%) following a review.
- 16% of firms have received an ILG following a SREP, which is broadly consistent year-on-year (2023: 20%).
- The median increase in capital requirements where firms are issued an ICG is 25%. This is significantly lower than the previous year where participants had a median increase due to an ICG of 37%.
- The median increase in liquidity requirements where firms are issued an ILG is 12%. This is lower than the previous year where participants had a median increase due to an ILG of 28%

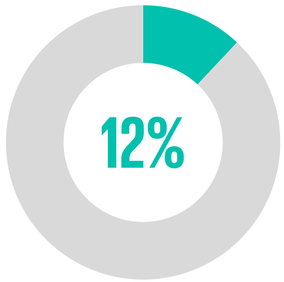
Outcomes of FCA SREP reviews since the IFPR came into force



Median impact of a capital add-on under the IFPR



Median impact of a liquidity add-on under the IFPR



KPMG View

Now that the FCA has completed their reviews of the first round of firms subject to the IFPR, there is a clear trend of firms being less likely to receive capital or liquidity add-ons compared to the previous regime. Even where issues are identified, the overall capital impact of these appears to result in smaller increases than previously seen for firms subject to prudential supervision by the FCA.

However, where the FCA does identify weaknesses in capital and liquidity assessments, we have seen a trend of greater use of Risk Mitigation Plan actions to ensure firms appropriately address feedback. In our experience, these actions typically include granular steps firm must take to remediate issues and typically require reviews and attestation from Senior Management and Internal Audit functions.

We expect future FCA reviews to focus on the largest firms (who will always pose a risk to clients and the market) and on more targeted reviews of medium and small sized firms where there are firm specific or thematic issues impacting certain sectors.

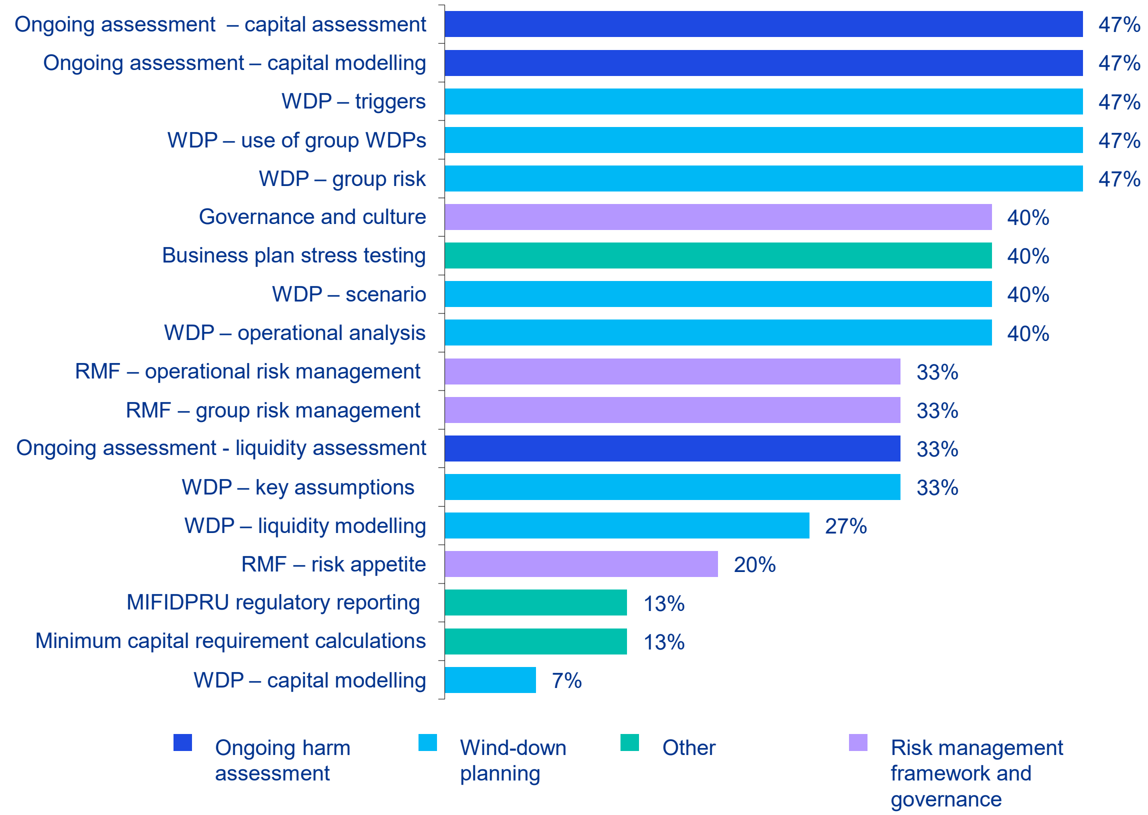
Key areas of FCA focus during the SREP

FCA feedback to the majority of firms focussed on their ongoing harm assessments and their WDPs.

Trends in the data

- The previous years results highlighted Wind-Down Planning as the most common issue raised as FCA feedback in our survey. In 2024, the ongoing harm assessment (87%) is now the most common issues raised during the SREP.
- Where firms received feedback on their ongoing harms assessment, the FCA highlighted capital modelling (43%), liquidity assessments (43%), the use of statistical models (35%), and business plan stress testing (35%).
- Other commonly raised points focused on Risk management framework (57%), governance (35%) and business plan stress testing (35%).
- Only 9% of survey participants subject to a SREP received feedback on their MIFIDPRU regulatory reporting.

Proportion of respondents stating they received FCA feedback on the following areas as a result the SREP



KPMG View

For many firms, their SREP reviews were predominantly through desktop documentation reviews of the ICARA, WDP and supporting documents. The FCA also interviewed key personnel associated with these assessments. However, this approach meant there was significant focus on the quality and completeness of a firm's ICARA document and Wind-Down Planning. Given the key parts of these assessments were identified as the most common areas of FCA feedback, this likely reflects areas of FCA focus during these reviews.

In our experience, weaknesses in more technical areas (i.e. the ICARA and WDP) were also linked by the regulator to broader points around the Risk Management Framework and Governance. Therefore, either the regulator is more likely to do broader analysis where issues in the ICARA and WDP are identified or firms with these issues are more likely to also have Risk Management Framework or Governance weaknesses.

Going forward, we expect the FCA to perform specific thematic reviews on areas they see as higher risk (for example, for firms going through significant growth) and to assess how firms have responded to, and implemented, the published recommendations from their reviews to date.

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CREATE: CRT159424 | February 2025