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The FCA's Smaller Asset Managers and Alternatives Business Model Review

Stuart Holman May 12, 2025

On 8th May 2025, the Financial Conduct Authority ("FCA") published the results of its review of business models for smaller asset managers and alternative investment firms and found most of the firms it reviewed were meeting its expectations.

The review was conducted via questionnaire over three phases (April 2023, November 2023 and September 2024) and covered 410 firms, each with assets under management (AuM) of less than £1 billion—a significant proportion of the 1,100 firms in that segment of the industry.

Upon receiving the responses from the 410 firms, the FCA selected 60 for a more in-depth assessment. The FCA chose these firms based on business models of interest to the FCA, their retail exposure, and whether they offered high-risk investments (HRIs). Where the FCA identified weaknesses, firms received feedback, and in some cases, the FCA applied "regulatory tools" to mitigate material risks of consumer harm.

The review focused on three key areas:

High-Risk Investments

The effectiveness of firms' product governance, the clarity and compliance of their financial promotions, and the processes used to assess and categorise investors or clients to ensure adherence to marketing restrictions for high-risk investments (HRIs).

Conflict of Interests

The control practises within firms to manage conflicts of interest.

Consumer Duty

How firms have embedded the Consumer Duty into their activities.

The FCA's Findings

High-Risk Investments

The FCA focused on how these firms adhered to the rules on financial promotions and communications, including the marketing restrictions for HRIs set out in COBS 4. It sought information from firms offering Restricted Mass Market Investments (RMMIs) and Non-Mass Market Investments (NMMIs), with specific reference to the rules in COBS 4.12A and COBS 4.12B.

The FCA found that while most firms offering HRIs were able to categorise their products as either RMMIs or NMMIs, some could not clearly explain the distinction between the two or how to apply all components of the customer journey for HRIs as outlined in COBS 4.12A and 4.12B. Additionally, many firms demonstrated insufficient understanding of retail investor categorisations—such as high-net-worth, sophisticated, or restricted investors—placing them at risk of non-compliance with marketing restrictions designed to protect more vulnerable investors.

Financial Promotions

The FCA also identified instances where firms used unclear risk warnings on their websites and social media platforms. Additionally, it found cases where firms were unable to explain likely investment returns and provided incomplete disclosures of investor costs.

Elective Professional Clients

The FCA assessed how firms conducting opt-up processes adhered to the relevant requirements. The regulator found that some firms relied on qualitative assessments with a limited number of questions, unclear pass/fail criteria, or overly simplistic confirmatory questions. Additionally, some firms lacked a clear process for handling clients who no longer met the conditions required for categorisation as an Elective Professional Client (EPC).

The FCA directed that it expects firms to:

- Use structured assessments to evaluate EPC criteria;
- Clearly document all testing, risk warnings, and declarations prior to onboarding; and
- Implement post-onboarding processes to ensure they meet their recategorisation obligations.

Appropriateness Assessment and Preliminary Assessments of Suitability (PAoS)

The FCA found that smaller firms offering HRIs to non-advised retail investors often lacked sufficiently robust processes for conducting investor assessments or misunderstood the differences and applicability of various assessment types. Additionally, some assessments were not sufficiently challenging or failed to include questions tailored to the specific risks of the investment.

There were even instances where firms were found to have bypassed their own controls to help investors pass assessments.

In its findings, the regulator provides useful guidance to firms on how to create financial promotions that meet its expectations, implement appropriate product and investor/client categorisation procedures, and carry out adequate investor assessments.

Conflicts of Interest

The FCA acknowledged that smaller firms often operate with more condensed business models, resulting in senior staff taking on multiple roles. This naturally presents potential conflicts of interest. As such, the FCA examined the effectiveness of the governance and conflict mitigation policies these firms had in place to manage conflicts that these firms could not avoid.

While most firms had conflicts policies, some lacked procedures tailored to their specific business models, investment strategies, underlying product structures, or the involvement of individuals and third parties. The FCA also found that conflict registers maintained by these firms were not always up to date or sufficiently detailed to log conflicts, outline mitigation strategies, and explain ongoing monitoring arrangements. Furthermore, some firms lacked clear processes for identifying and assessing all potential conflicts.

The FCA also identified instances where firms failed to clearly disclose unmanaged conflicts to investors.

Once again, the FCA provided useful guidance on good practices for managing conflicts—guidance that firms of all sizes and business models should review.

The Consumer Duty

The FCA reminded firms that encouraging customers to seek professional client status solely to avoid providing the protections afforded to retail clients constitutes a breach of the Consumer Duty.

The FCA found that some firms had still not considered how the Consumer Duty applies to their business models and, as a result, had not embedded the necessary processes to comply with their obligations. The regulator emphasized that any firm that has not yet done so must act urgently.

Additionally, the FCA found that some smaller firms—despite the principle of proportionality—were not preparing meaningful Consumer Duty board reports. These firms were also unable to demonstrate effective challenge from their governing bodies and senior management in relation to these reports. The regulator reminded firms of its published findings on Consumer Duty board reports from December 2024, which include suggestions on how smaller firms can enhance the quality and effectiveness of their reports.

What should firms do now?

While the FCA's review focused on asset managers and alternative firms with assets under management below £1bn, it expects that some of its findings may also apply to larger firms in the sector.

The FCA directs that boards or management committees should review this publication to:

- Identify and manage key risks of harm.
- Deliver good outcomes for consumers.
- Support confident investing and economic growth.

The regulator also announced that it will continue to monitor firm conduct on these topics, including through subsequent tranches of this questionnaire, with a particular focus on our supervisory priorities as set out in the portfolio letter, Asset Management and Alternatives (February 2025).

How Waystone can Help

If your firm would like any assistance in meeting the regulatory expectations set out in the FCA's findings, please contact us through the following link:

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