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BVCA response to HM Treasury's Call for Evidence on the Financial Services Growth & Competitiveness Strategy

The British Private Equity and Venture Capital Association (BVCA) is the industry body and public policy advocate for the private capital (private equity, venture capital and private credit) industry in the UK. With a membership of over 600 firms, we represent the vast majority of all UK-based private capital firms, as well as their professional advisers and a large base of UK and global investors.

We are pleased to share with HM Treasury the BVCA's submission to the Financial Services Growth and Competitiveness Strategy. The BVCA welcomes the Government's commitment to growth economic growth, boosting economic stability and increasing investment in the UK.

In order to contribute to this overarching aim of economic growth, the financial services industry needs to ensure the right policy environment to boost investment. The Financial Services Growth and Competitiveness Strategy underlines the Government's understanding of the vital role of the financial services sector in achieving this, and we welcome the opportunity to contribute to the development of the Government's thinking in this area

The private equity and venture capital (private capital) industry is an indispensable partner for UK economic growth, standing as it does at the unique intersection of deploying capital, investing for the long term and helping to shape the strategy of the British businesses it invests in. In 2023 alone, it directly supported 12,000 businesses, generating 2.2 million jobs and contributing 6% to GDP across all sectors.

UK-based private capital specialists currently have **£178 billion of funds raised to invest**, which they expect to **deploy in the next three to five years**. Historically, around half of these funds managed in the UK, known in the industry as 'dry powder', are put to work here in British businesses.

Capital is mobile. To drive economic growth, we must bring that capital here, both by encouraging the global investors to put their capital in UK funds and by ensuring that investors have the confidence to invest in UK businesses.

<u>BVCA responses to HM Treasury's questions</u>:

Question 3.1: Do you agree with the proposed objectives:

In the context of the focus on growth and competitiveness, the government's proposed objectives for the strategy are to deliver a credible 10-year plan that will ensure the UK:

- **is a place where financial services firms can invest and grow with confidence, and the location of choice for international firms;**
- **supports the start-up and scale up of innovative new types of financial services;**
- **provides financial services firms with access to a highly-skilled workforce;**
- **has sustainable growth in the financial services sector across all regions and nations;**
- **continues to be a world leading sustainable finance centre and the global destination of choice for firms to raise green capital; and,**
- **takes advantage of new export markets while maintaining existing strengths, increasing its global share of financial services exports.**

Yes, broadly, the BVCA agrees with these proposed objectives. The Government's driving objective should be to return the UK to economic growth, boosting economic stability and increasing investment in the UK.

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In order to contribute to this overarching aim of economic growth, the financial services industry needs the right policy environment. In our Manifesto, published in May 2024, the BVCA set out four guiding principles which we believe should drive the Government's approach:

1. **A stable economy**, with macro-economic conditions conducive to investment and growth.

2. **World-class regulatory standards** which are applied proportionately and do not disadvantage businesses seeking private capital investment.

3. **Support for an investment ecosystem** that attracts global investment talent and maintains the UK's competitive advantage in private capital.

4. **Predictable policy frameworks** that provide confidence that investment in different sectors of the economy today will be supported and taxed consistently throughout the ten-year (or more) lifetime of a typical private capital fund investing for the long-term.

The private capital industry is already an indispensable partner for UK economic growth, standing as it does at the unique intersection of deploying capital, investing for the long term and helping to shape the strategy of the British businesses it invests in. In 2023 alone, it directly supported 12,000 businesses, accounting for 2.2 million jobs and contributing 6% to GDP across all sectors.

Question 3.2: [For Financial Services Organisations] For firms operating in more than one jurisdiction, what are the main drivers affecting your decisions on where to invest?

As the industry body and public policy advocate for private equity and venture capital (private capital), the BVCA has been the voice of private capital in the UK for over four decades. With a membership of over 600 firms, we represent the vast majority of all UK-based private capital firms, as well as their professional advisers and a large base of UK and global investors. Although we are not a firm looking at where to invest, BVCA research and reports have considered some of the key drivers and barriers to investing in the UK.

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UK based private capital specialists have £178 billion of funds to invest, which they expect to deploy in the next three to five years. Historically, around half of the funds managed in the UK, known in the industry as 'dry powder', are put to work here.

Capital is mobile. To drive economic growth, we must bring that capital here, both by encouraging the global investors to put their capital in UK funds and by ensuring that investors have the confidence to invest in UK businesses. Earlier this year, the BVCA and Public First set up the Investment Commission, bringing together a range of experts representing investors, business leaders, academics, think tanks and business groups, to recommend changes that would result in a greater share of dry powder being invested in the UK.

To support its work, the Investment Commission conducted two surveys of BVCA members, held one-to-one interviews with senior investment professionals, and convened expert roundtable discussions on three specific themes: green transition and clean energy, the UK tech sector, and investment in the nations and regions of the UK.

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The Investment Commission identified seven barriers to investing in the UK, which we outline below with accompanying evidence. These barriers cut across growth-driving sectors and industries.

Barrier 1: Policy uncertainty

Political uncertainty and frequent unpredictable changes of policy damage the confidence of investors and create problems for the UK businesses they invest in. Capital is mobile. Government needs to think about the messages it is sending not just to voters but also to people who are considering making large, long-term investments in the UK, and who could make those large, long-term investments in businesses based elsewhere instead. In our BVCA member survey, we found that 71% say UK businesses they invest in have experienced problems because of political or policy uncertainty, and 33% say a clearer net zero and policy roadmap would make it easier for them to invest in a UK business.

One investor told us: *"If you want people to invest in the UK, they have to understand what the long term intention of the UK Government is, or what long term policies are, and I just don't feel that our politicians and governments currently think in that 20, 30, 50, 100-year time plan, it's much more short term than that. And that's challenging for us if we're having to invest in 50, 60, 70 year assets, or assets where just to get them constructed and permitted could take 5-10 years, and if policy changes within that timeframe, then we're on the wrong end of that."*

Barrier 2: Complexity around regulation and incentives

Investors told us that complex regulation and uncertainty over incentives can make other nations a more appealing destination for investment. A simple message about predictability of return on investment and Government support, along with clarity about who to engage with, really matters. In our BVCA member survey, we found that 42% of respondents have decided not to invest in a UK business because of regulatory uncertainty, and 50% say reform of the British Business Bank to support larger-scale investments or invest more flexibly would make it easier for them to invest in UK businesses.

Both the Inflation Reduction Act (IRA) in the USA and the very differently-structured EU Green Deal were mentioned as initiatives that potential investors could navigate relatively easily, compared to opportunities for UK government support for investment. The precise level of particular taxes is not investors' only consideration: where tax rates in a particular country have been highly stable over decades, investors can build that predictability into their assumptions when assessing likely returns, meaning that tax stability provides a comparative advantage in itself.

Barrier 3: Planning delays

A major uncertainty facing investors, and the businesses they invest in, is the length of time it can take to get planning permission for facilities they are ready and willing to pay for, such as factories and labs, but cannot build without approval. In many cases, their plans are also vulnerable to planning delays affecting other necessary infrastructure, both public and private, from the grid to transport to housing. For example, a lack of housing in certain areas has a direct impact on workforce capacity, which again impacts the viability of investments. In addition to the need for planning reform to remove blockages and delays to necessary infrastructure, there is a basic problem of capacity within the system, with both additional resources for planning departments and additional planning staff required to meet demand. In our BVCA member survey, we found that 35% of respondents say businesses they invest in have experienced problems because of planning delays, and 33% say planning reform would make it easier for them to invest in UK businesses.

Barrier 4: Poor public infrastructure

Some of the most important factors that affect whether an investment will deliver a return are beyond the control of either investors or the businesses they invest in, but are either in the direct control of government or subject to long-term government decisions: grid connections that affect whether a new manufacturing facility can operate; transport links that affect where the workforce can be drawn from. This is separate from the question of whether public investment can "crowd in" private investment in related sectors; it is about public infrastructure that creates overall national capacity and, in the case of transport infrastructure, especially regional capacity for businesses to attract investors.

In our BVCA member survey, we found that 42% have decided not to invest in a UK business because of a lack of public infrastructure such as transport or grid connections, 43% say that significant public investment in green energy would make it easier for them to invest in UK businesses, and 34% say that significant public investment in transport infrastructure would make it easier for them to invest in UK businesses.

Survey respondents also cited a lack of investment in the regions and in transport and other infrastructure as major barriers to investing outside London and the South East:

"When you talk about how easy is it to get an investor to visit somewhere outside of London, well, when you tell them that it's two hours on a train, and the chances are it won't turn up, or you won't get back afterwards, that becomes a huge problem. And that is a macro decision that was taken, which is public investment has been massively focused in London and the southeast."

Barrier 5: Domestic workforce skills shortages

Skills shortages in the recruitment of their domestic workforce were identified by investors in our survey as the single biggest issue for UK businesses they invest in, and a major factor in deciding not to invest in particular UK businesses.

The Investment Commission also heard that management teams often lack some of the specific skills and expertise they need, especially in SMEs with limited resources, to deal with the newer challenges they are being asked to meet.

In our BVCA member survey, we found that 79% say UK businesses they invest in have experienced problems as a result of skills shortages in the recruitment of their domestic workforce, and 25% have decided not to invest in a UK business as a result of skills shortages in the recruitment of their domestic workforce.

In some cases, they said they were in a position to attract people with the right skills from other sectors – for example, people who can move from real estate development to renewable energy development – but noted that those sectors were also nationally important and in need of the same skilled workers, pointing to a recruitment problem that goes beyond the needs of any specific business or investor or sector. Support for skills training programmes that focus on particular skills gaps would make it easier for businesses to be confident that they can recruit the workers they need, and for investors to back them.

Barrier 6: Recruiting global talent

The UK is not the only country seeking to attract investment. New visa schemes elsewhere in Europe are making it easier for talent in the tech sector in particular to settle in other countries for longer periods at a lower cost. Small teams at venture capital and some growth equity firms, start-ups and SMEs often lack in-house expertise in international recruitment and immigration rules, and are forced to rely on expensive external advice: streamlining the visa application process for these firms would make it much easier to attract and retain talent in the UK.

In our BVCA member survey, we found that 68% say a less restrictive immigration regime for global talent would make it easier for them to invest in UK businesses, and 11% have decided not to invest in a UK business because of barriers to access to global talent.

Barrier 7: Lack of regulatory agility in innovative sectors

Many tech startups in particular are working with innovative technologies – from AI to medical devices to quantum technology to driverless cars to novel foods – which are rightly subject to regulation but where their regulatory status is unclear, because regulations have not kept pace with what is now technologically possible. This makes it much more difficult for investors to understand what their return on investment is likely to be, whether a product has a path to market and how quickly it will get there, and indeed whether a business is viable at all.

In our BVCA member survey, we found that 91% of respondents say a faster and more agile regulatory system would make it easier for them to invest in UK businesses. Government should build on the launch of the Regulatory Innovation Office and conduct a cross-cutting review of regulation of innovative technologies, focused on areas where regulatory capacity is holding back innovation and growth, and where legislation has not kept up with technological possibilities.

The BVCA Investment Commission report can be found here.

Question 3.3: What do you consider to be the most important trends or changes likely to affect the financial services industry over the next 10 years?

Below we have set out what we consider to be important trends and changes likely to affect the private capital industry in the next decade, and included some high-level recommendations on how we believe policymakers should react to them:

1. **Gravitation of asset management and capital markets towards private capital**

    The growth of the private capital industry has been fuelled by more companies remaining private or remaining private for longer. This means a greater amount of economic growth is only accessible to investors via private capital. 6% of UK GDP is delivered by private capital-backed companies (10% of private sector GDP), which also tend to operate in innovative and fast-growing sectors, such as technology and life sciences. BVCA data shows that the average investment period for private capital is 5.5 years, in contrast to less than a year in public markets. As of December 2023, UK private capital funds delivered returns of 15% compared to 5.3% for the FTSE All Share and 7.5% for the MSCI Europe index over the same period a 10-year horizon. In the UK, of all businesses with more than 50 employees, less than 4% are publicly listed on the London Stock Exchange.

    All this means that traditional asset managers and capital markets participants are increasingly seeking access to private capital through new products and partnerships (or by acquiring specialist private markets businesses), and large private capital firms are diversifying their own product ranges and partnering with institutions like insurers. We expect these trends to continue and the already complementary relationship between public markets and private capital to become even more so.

    In this context, we support the Government and FCA's work on establishing the PISCES framework. The sandbox process should aim to identify ways to minimise the burdens and increase the 'use cases' so that dynamic and liquid platforms can be established that encourage investment in UK growth companies and attract more overseas companies towards the UK. Equally, we urge the Government to view public markets and private capital as part of one

business financing ecosystem, and take a holistic approach to financial services policy development.

2. **UK and global firms expanding operations within the EU**

UK and global private capital firms increasingly favour the EU over the UK as the European region for the future growth of their operations. This is in part because they see establishing investment management firms, building out headcount and launching more funds in the EU as the most efficient way of maintaining access to European and UK investors because this grants access to the Single Market fund marketing passport, which allows funds established in the EU to be marketed to institutional investors across the EU. This approach also allows such EU funds to be marketed into the UK using the UK's flexible national private placement regime at negligible additional cost. Those funds can also be marketed to institutional investors in many other global jurisdictions. This results in Luxembourg/Ireland often being selected as the jurisdiction of choice for global fund offerings (or funds offered globally excluding North America).

The desirability of increasing headcount in the EU is driven in part by increasing focus on 'substance' requirements of local regulators (e.g. the Luxembourg CSSF and the Central Bank of Ireland) under EU AIFMD and for tax purposes. UK firms regulated as UK Alternative Investment Fund Managers (AIFMs) that establish an EU AIFM to maintain Single Market access need to obtain additional MIFID permissions in the UK (in contrast to firms located entirely in the EU which only need an AIFMD licence). This can be a significant burden given the additional requirements under UK MIFID, particularly the UK's Investment Firms Prudential Regime (which has had a disproportionate impact on private capital firms, contrary to the intent of the framework).

Whilst the UK remains the largest single European jurisdiction for private capital management staff, new growth is primarily focussed in the EU, with Ireland and Luxembourg being the primary beneficiaries. It is worth noting that the attractiveness of the UK for internationally mobile individuals pursuing a career in private capital is already under the spotlight due to the planned changes announced at the Budget to the taxation of carried interest in the UK, the abolition of the non-dom regime (albeit with the introduction of the FIG regime) and the changes to inheritance tax rules. These changes combine to make other European jurisdictions relatively more attractive. This puts further pressure on the regulatory issues identified above and highlights the need for financial services taxation policy to support wider UK competitiveness. All of this means more of firms' activity happening in the EU instead of the UK (so it is important for the UK to find ways to use the regulation and other levers to ensure the UK remains competitive).

For the UK to reverse these trends, the UK would need to have an arrangement with the EU so that UK fund structures could be marketed across the EU. The UK would also need fund structures which meet the needs of global investors from a tax and commercial perspective (alongside the positive steps already made through the QAHCs regime for investee company holding structures). In the absence of the former, it is not necessary for the UK to maintain full alignment with the EU AIFMD regime. The UK should find ways to maintain partial alignment to support arguments for EU market access whilst also allowing the UK market to evolve and maintain its competitive edge on the global stage. This is why the BVCA has recommended an opt-in approach and greater proportionality for the review of the UK's AIFMD framework in 2025.

3. **Geopolitics favouring more local investment**

There is increased competition between jurisdictions to attract private capital investment into their domestic economies. Governments will increasingly attempt to ensure domestic investors in their jurisdictions (such as pensions and insurance companies) invest more in their own economies. Evidence of this trend can be seen in various current developments, such as the UK pensions agenda, the US tilt towards protectionism (and its development of a new national security screening regime for outbound investment), the centrality of EU economic competitiveness to the new Commission (e.g. the Draghi report), the ongoing debate in Canada about Canadian pensions investing more in the Canadian economy (mirroring the UK discussions).

The Government should continue its determined focus on increasing UK pension investment in UK companies, remembering that smaller private capital funds in particular are critical motors of SME growth across the UK, and encourage the FCA to revisit its "Permitted Links" rules to make it easier for DC pensions investing through life insurance platforms to access the full range of private capital funds. Equally, the UK clearly benefits from its position as a global hub for private capital investment, which means the Government should ensure UK regulation facilitates global institutional investment in funds managed by UK private capital firms and to argue on the international stage in favour of the free flow of capital.

These developments also threaten to accelerate the trend of cross-border M&A activity becoming more complicated as new transaction clearances are brought in, which the UK should be careful not to exacerbate unnecessarily.

At a more granular level of locality, private capital investment will also grow continue to grow in importance for the UK's national and regional economies, particularly as policy initiatives aimed at improving UK universities' ability to capitalise on IP through spin-outs take root. This means the Government should focus on understanding and nurturing the growth of local/regional innovation and investment ecosystems, and ensuring that UK investors are able to access investment opportunities through small private capital funds (particularly relevant for the LGPS, which are well-placed to support the UK's national and regional economies).

4. Growing demand for private capital from sophisticated retail investors

There is extremely high demand for private capital investment opportunities globally from family offices, HNWI investors and wealth management/private bank clients. Firms are rapidly increasing their ability to offer products for these investors, generally semi-liquid evergreen funds domiciled in the EU. Luxembourg is the clear European leader in this space and the EU is also re-energising the European Long Term Investment Fund (ELTIF) which is expected to further accelerate EU leadership in this space.

The UK should take this into account when considering the effectiveness of its sophisticated retail investor marketing rules, their interaction with UK MiFID and the LTAF framework (a relatively new fund vehicle for which the FCA should conduct a post-implementation review looking at retail investment in private capital). This, alongside reducing frictions for the distribution of non-UK domiciled private markets funds to UK individuals, would help firms based in the UK to raise pools of "retail" funding in the same way many of them are successfully already doing in other markets, such as the US and Europe.

5. Growing investor demand for SMEs to provide ESG data

Institutional investors invest in both public markets and private capital. In order to compare the ESG credentials of these two types of asset, investors increasingly request similar data from

private capital firms to that available in public markets. The challenge comes from the fact that public markets investments are in large public companies with the resources and systems to provide detailed ESG metrics, whilst private capital investments are in unlisted, fast-growing SMEs, which do not have the same level of resources and for obvious policy reasons are not subject to the same reporting requirements as large listed companies. The risk is that private capital-backed companies may struggle to demonstrate their ESG credentials, even though private capital investment is more likely to have positive impact and ESG outcomes.

The active ownership model, combined with more frequent injections of productive capital, enables private capital firms to make a strong positive contribution to investee companies' ESG performance during the period of ownership. Private capital firms have the longer term perspective, expertise and networks needed to improve ESG performance. They also have strong incentives to do so, because they need to know their funds' portfolio companies will be sustainable for future buyers (when the companies are sold, on average after a 5.5-year hold period). Investing in environmental and social solutions and growing companies that are resilient to tomorrow's world is thus a value creation exercise that leads to higher price on exit, and therefore higher returns for investors.

Policy must therefore support SME growth by ensuring appropriate thresholds are maintained so that smaller companies are not overburdened by disproportionate investor or regulatory data requirements and that the sustainability impact driven by private capital investment can be reflected in reporting and factored into investors' allocation decisions. Proportionality and materiality are the watchwords here, and the Government should ensure that the incoming ISSB framework encourages convergence, consistency and usefulness of data collection in a way that drives meaningful sustainability outcomes that are relevant to individual businesses and their growth stage. The UK must also remain conscious of the global interconnectedness of the UK private capital industry and prioritise 'interoperability' between different jurisdictions' sustainability reporting frameworks so that UK regulation in this area does add to the case against firms locating themselves here.

6. **Growing demand for sustainability-focussed investment strategies (e.g. impact investing) and the role of private capital in the green transition**

   Investors of different types, often driven by demand from their own clients or beneficiaries, increasingly seek allocations to assets which can help them demonstrate a positive impact of their investment strategy on social and environmental objectives (in particular impact investment strategies), although investor focus on ESG varies per jurisdiction with e.g. certain US investors taking an actively "anti-ESG" approach, which is a consideration that private capital funds which typically have a global investor base need to navigate (as does UK regulation).

   This 'investor contribution' to sustainability objectives is often more readily achieved through private capital investment. This is because of the active ownership model firms use to create value within portfolio companies and the capital injections that often follow from an investment by a private capital fund. The significant influence that private capital firms' large or controlling ownership positions mean they exercise over their funds' portfolio companies allows them to use a sustainability lense to facilitate value creation - private capital investments provide both an opportunity and an incentive for firms to drive real economy sustainability improvements in a way that is difficult to achieve through typically smaller and more intermediated holdings in public companies traded on the secondary market (hence the importance of the Stewardship Code to influence company behaviour in the public markets context).

Policy interventions need to recognise the importance of private capital investment to developing the green technology required for transition. Private capital funds invest in the solutions of tomorrow - green technology is often nascent, unproven and therefore often more risky. Industry therefore needs policy certainty on proven technologies to help them scale, create investor confidence and provide financial solutions through blended finance mechanisms to reduce that risk. Policy must also recognise the role of private capital in driving down carbon emissions amongst UK SMEs (90% of companies backed by BVCA members are SMEs, and SMEs are collectively responsible for 50% of the UK's business emissions, according to the British Business Bank). This is why the BVCA has shared with officials a range of detailed policy recommendations for Government action to maximise the private capital industry's contribution to the green transition.

7. **Greater use of AI and other tech in firms' operations**

Private capital firms, including venture capital firms, are often very much involved in the funding and growth of technology, and increasingly adopting more automated process and AI into their own operations. The range of applications of this technology is growing across many areas, including due diligence, cutting costs, increasing productivity and enhancing compliance processes.

Private capital firms have a front row seat and are an active participants in these cutting-edge AI and other tech developments. This means BVCA members are well-placed to share lessons across investee companies, with policymakers and more widely. The Government should seize the opportunity to engage with private capital to help the UK cultivate innovative AI companies which will offer attractive funding opportunities to UK and international investors through the UK's world-class venture capital funds.

8. **Increased interest in private capital from policy makers and public**

The continued growth in size of the private capital industry, in the UK and globally, already is and will continue to attract increased amount of policymaker, press and public questions about how the industry works. Private capital is important for investors – the industry's returns as a whole have consistently exceeded those of public markets for decades (the range of evidence for this is summarised here). But private capital investment is also important for the UK economy - 6% of UK GDP is delivered by private capital-backed companies, which also tend to operate in innovative sectors, driving innovation and productivity, and are likely to play an increasing role in the provision of certain public services e.g. healthcare.

Understanding the impact of private capital investment and how it creates value is vital for policy-makers, and the industry must ensure this value creation is better explained. At its most basic level, private capital invests in businesses with the aim of achieving a return on their investment. That means adding value: ensuring that the business is worth more at exit than at the time the initial investment was made. In order to achieve this, investors want to improve productivity, profitability and growth - in brief, making businesses better. Private capital ownership improves productivity, and incentivises operational improvements, business evolution and expansion as part of value creation that drives returns (especially now the interest rate environment appears to have reduced the impact of rationalising companies' capital structures).

Recent analysis finds that private capital ownership has a long-term positive impact on business productivity, compared to non-private capital backed businesses, and that private capital-backed firms' productivity is more resilient during economic downturns such as the global financial crisis and the Covid-19 pandemic. Further details of this can be found on the BVCA's research hub.

The Government has already acknowledged the importance of boosting productivity to support economic growth. The BVCA and Public First looked further into what private capital investors actually do to improve the productivity of the companies they invest in and create more value, identifying key techniques and tools that private capital owners deploy. Further details can be found here.

It is primarily the responsibility of the industry to ensure that it communicates effectively and openly with wider stakeholders. Policymakers and regulators also have a role in ensuring that regulation of the industry is based on strong understanding of the commercial and technical characteristics of private capital funds and their contribution to UK economic growth and public service provision. The BVCA is keen to continue assisting policymakers in developing this understanding, building on our ongoing engagement with politicians, government officials, the FCA and the Bank of England.

9. **Greater demand for liquidity from private capital investment**

The growth in size, sophistication and maturity of the private capital fund management industry is already leading to growth and innovation of investment strategies and products, in particular to adapt to the growing demand from institutional (and, increasingly, sophisticated retail) investors for more liquidity options. This includes secondaries funds, open-ended evergreen funds and continuation funds, and is a trend that has been a focus of the UK DC pensions market which has specific liquidity considerations. This diversification of offerings is a positive development and a sign of a maturing and growing market. It is important for the UK economy that Government and regulators recognise this trend as such (for more detail see the BVCA's submissions to the Bank of England on financial stability considerations).

10. **Growth of private credit funds**

The significant growth of the private credit fund sector over the last decade (estimates of the total size of the private credit market lie between $2tn and $3tn worldwide), fuelled to some extent by a (regulatory-driven) reduction in bank participation in lending to private companies since the financial crisis, has been vital for the UK economy and has made a positive contribution to the financial system. Without private credit funds, many private companies would have found it extremely difficult to raise capital.

Private credit functions in partnership with private equity investment, with both focused on business growth. Private credit can provide more flexible, quick, long-term and dependable direct lending to companies than traditional banks, and at different stages of their growth cycle, as well as strong risk-adjusted returns for investors. Private credit funds, unlike banks, do not suffer from liquidity mismatch issues, and are countercyclical investors, much less leveraged, more resilient and diversify risk thereby enhancing financial stability.

The growth of private credit is set to continue and the importance of this specialised, direct lending activity to UK businesses and the economy must be reflected in UK policymaking - prudential regulation in particular must clearly recognise that private credit funds should not be regulated like banks.

Question 4.1 Do you agree with the list of policy pillars that the government intends to focus on? Are there other areas that should be included?

- Innovation & Technology: enabling and supporting increased digital adoption, including technologies such as Artificial Intelligence (AI), which have the potential to increase productivity and open up new products and services.
- Regulatory Environment: ensuring there is a robust and transparent regulatory framework that supports growth while also maintaining financial stability, ensuring that markets function well, protecting consumers and promoting competition.
- Regional Growth: promoting growth across all regions to ensure the benefits of the UK's financial sector are felt by citizens nationwide.
- Skills & Access to Talent: ensuring a strong pipeline of homegrown talent and that the UK remains an attractive destination for top talent internationally.
- International Partnerships & Trade: maintaining the UK's success as a global financial hub through strong trade arrangements and international leadership on financial regulation.

As flagged in question 3.2, the BVCA and Public First identified seven barriers to investing in the UK which feel relevant here. Our recommendations, as shared above, fit within the categories listed, and we would emphasise in particular:

- The need to reduce complex regulation and uncertainty over incentives.
- The need for regulatory agility in new and innovative sectors.
- The importance of resolving challenges around planning and public infrastructure to improve regional investment.
- The importance of a visa regime that allows financial services firms to bring in the most talented individuals in a fast and simple manner.

The BVCA Investment Commission can be found here.

Question 4.2: Please rank the list of pillars in order of importance to your business or organisation for:

i) day-to-day operations
1. Skills & Access to Talent
2. Innovation & Technology
3. Regulatory Environment
4. Regional Growth
5. International Partnerships & Trade

ii) ii) longer-term plans for investing in the UK:
1. Regulatory Environment
2. International Partnerships & Trade
3. Regional Growth
4. Innovation & Technology
5. Skills & Access to Talent

Question 4.3: How well is competition currently working in the financial services sector, and how can it be improved?

Competition in the private capital sector is healthy, with a large number of firms, both large and small, located in the UK. There are many aspects of the UK that makes it a real hub for private capital investment and gives it a reputation as a world-leading location for businesses to start up and grow. There is a vibrant financial services centre, world-leading legal system, dynamic research and development sectors; and

clear and long-standing ambitions to attract global investment and grow UK businesses. In 2023, private capital invested £20.1bn into UK businesses, generating 6% of UK GDP. Companies backed by private capital employed 2.2m people across the UK.

The private capital investment model is straightforward (raising funds, investing them over several years in unlisted companies, using their influence to improve those companies to generate returns for investors on exit). However, the technical "plumbing" behind this activity is often extremely complex because private capital needs to accommodate different types of investors from around the world. The private capital industry will only remain attracted to the UK if the country's tax, legal and regulatory frameworks for private capital fund management are flexible enough to allow capital to flow efficiently through UK structures, while maintaining robust standards demanded by the most sophisticated institutional investors in the world.

There are specific risks of adverse effects on competition in the audit and non-audit financial services sector if the Government continues with proposals to expand the public interest entity (PIE) definition in its upcoming legislation on corporate governance and audit reform.

The BVCA has always supported measures to improve quality and independence in the audit market. An important part of the private capital business model is to build robust and effective governance structures, fostering growth and innovation and creating long-term value, as demonstrated by many academic studies. The private capital industry is committed to additional governance and transparency, and examples of this in practice include the BVCA's work on the Wates Principles for Large Private Companies and the Walker Guidelines, implemented and monitored by the Private Equity Reporting Group ("PERG"). This year, the PERG have undertaken a "root and branch review" of the Guidelines to ensure that they are up to date given changes in reporting requirements and expectations of transparency from public and private companies. Companies covered by the Walker Guidelines already comply with some of the requirements currently applicable to PIEs.

A clear and proportionate definition for a private company PIE is essential, including when and how a company might come into/out of scope of being a PIE. It is also vital that the Bill includes the FRC Ethical Standard (ES) private equity carve out in proposed corporate governance and audit reform legislation, to allow for sufficient competition and choice in the non-audit services marketplace. The carve out was included in the FRC ES following a review in 2019 and engagement between the BVCA and the FRC. Following its review last year, the FRC will amend its ES, which will remove the carve out due to the proposed expansion of the PIE definition. This will have an adverse impact on our members and their portfolio companies, removing choice in the market for non-audit services, and therefore limiting competition for a range of businesses – a clear divergence from Government intent to increase competition in the market.

The BVCA's response to the 2021 consultation on audit reform and corporate governance can be found here.

Question 4.4 What is your assessment of how effectively the UK supports innovation and the adoption of new technology? What could be improved in the financial services sector?

The UK has a strong track record in science and technology research but loses out on opportunities when companies move overseas, taking intellectual property, quality jobs, and innovation with them. Other issues related to lack of infrastructure further inhibit the UK from being a global scale-up destination for the largest tech companies.

While the UK has a strong funding ecosystem at the early stage, the 'scale-up' stage of VC investing often prompts UK companies to seek investments from the US and elsewhere. Innovative UK businesses

need this capital to create large-scale, independent, businesses, but relying on foreign investment to scale-up UK companies exposes the UK to geopolitical risk and fluctuations in global capital allocations.

The UK should be the best place to both start and scale a business. That means protecting our world class universities, having investor support for spin-outs and encouraging a greater appetite for risk taking at later stages to ensure companies can scale in the UK.

BVCA data shows that £8 billion was invested in UK venture capital in 2023, highlighting a strong year for a sector that fuels a diverse range of startups across the country. Our data also reveals British venture capital-backed businesses also added £20 billion in GDP to the UK economy in 2023, underscoring the vital role these companies play in driving innovation, supporting jobs, and economic growth.

But there is more to do in the UK to attract the investment that helps businesses start up, and significantly, continue to scale in the UK. The BVCA recommends the following:

- **Expanding the remit of the BBB:** to include lower mid-market PE funds, which will increase help increase the number of growth stage opportunities for direct investment, and help increase the attractiveness of initiatives (e.g. BGP) seeking to unlock pension fund investment.
  The British Business Bank's British Growth Partnership marks an important step to increase UK pension scheme investment into private capital funds. However, the BGP will be in the form of a co-investment model and while this is positive overall, it is harder to achieve scale quickly, given the limited number of co-investment opportunities and the challenge with ensuring investors are backing the best performing companies. There is also greater risk for institutional investors if they hold a less diversified investment portfolio. A fund of funds vehicle would be the best way to achieve greater diversification and access to higher returns from UK VC and growth equity funds.
  The Government and the BBB should build on the British Growth Partnership to establish new Government-backed vehicles and schemes, expanding the ambition beyond the "hundreds of millions" of additional capital sought by the BGP. This should consider a larger fund of funds program aimed principally at the LGPS and global investors seeking European exposure with a UK bias. This would allow the benefits from LGPS pooling to continue being realised at the same time as boosting UK regional investment from the LGPS and other investors through smaller UK private capital funds. Such a fund of funds program could deploy private sector expertise alongside the BBB. The Government has the legislative levers to encourage LGPS participation as well as the convening power used to such effect by the French Tibi scheme.

- **Ensuring regulation supports innovation:** Many tech startups work with innovative technologies, from AI to medical devices to quantum technology to fintech. It is of course right that regulators take a view on new technology to protect consumers and the wider economy, however in many cases rules have not kept pace with what is now technologically possible. This makes it much more difficult for investors to understand what their return on investment is likely to be and whether a product has a reasonable path to market, if at all.

  The FCA's sandbox is a valuable tool for innovation and the adoption of new technologies in regulated financial services by allowing firms to test their products in a controlled environment with guidance, mitigating risks and reducing uncertainty around compliance. While there are challenges, such as scaling innovations after testing and ensuring access and inclusivity for small firms, the FCA's sandbox is making a welcome contribution helping the UK in advancing its position as a fintech leader. We would welcome similar sandbox models being considered and rolled out by other regulatory authorities to provide innovators with testing ground and much needed regulatory support.

The UK's regulatory framework is often cited as a key challenge to enable effective speed to market for R&D commercialisation so it is positive that the government is setting up a new Regulatory Innovation Office. Regulatory checks are often cited as impacting investment activity.

- **Increasing the support available for R&D:** R&D (research and development) tax relief plays a very important role in the companies that are backed by private capital, particularly in businesses that are at the cutting edge of innovation such as deeptech and life sciences. The relief provides an efficient way of supporting companies to reinvest in their future growth. It is particularly important for early-stage businesses in the period before they start to generate income, as the availability of a payable tax credit increases the length of their cash "runway" (the amount of time for which they can operate before they run out of money). The UK economy needs these early-stage businesses to drive growth and employment for the future. Feedback from our members indicates that there are concerns both over the amount of the relief, and the way in which it is administered by HMRC. The BVCA recommends better resourcing of HMRC so that R&D claims may be processed quickly and fairly and greater transparency by HMRC over the sources of the "fraud and error" data that is used as the reason for burdensome HMRC checks into R&D claims.

- **Supporting innovation and entrepreneurs**: for example by helping to commercialise the Intellectual Property (IP) flooding out from UK universities through 'spin-outs', and keeping those businesses in the UK, is crucial to economic growth and creating jobs. The more growing businesses we have, the more investment opportunities there are. The stronger the UK can make its domestic pipeline of promising businesses, the more the country will attract private capital firms to expand their teams and investment activities here.

Question 4.6: What is your assessment of the UK's current regulatory environment?

The UK is currently home to one of the largest private capital hubs in the world, second only to the USA. Key to the UK's success in attracting private capital firms and global institutional investment capital over the last forty years has been its stable and robust regulatory framework. The UK's regulatory environment has been competitive and in line with the international standards demanded by global institutional investors. Historically, the UK's language accessibility, highly developed financial infrastructure and cultural appeal also made it an ideal location for global private capital firms to access EU investors and markets. To preserve the UK's position as a global hub for private capital management and investment activity, the regulatory regime must adapt to remain effective and attractive.

Private capital firms are solo regulated by the FCA as Alternative Investment Fund Managers (AIFMs) and/or Markets in Financial Instruments Directive (MiFID) firms, depending on the nature of their activities. The BVCA has good engagement with relevant FCA policy and supervisory teams, with clear points of contact. Broadly speaking, the FCA is well-respected amongst BVCA member firms and compares favourably to some regulatory authorities in key competitor jurisdictions. However, more can be done to improve regulated firms' experience and engagement with the FCA and to enhance the international competitiveness of the UK regulatory regime.

While it is too early to fully assess the effectiveness of the FCA's secondary international competitiveness and growth objective (SICGO), we welcome the regulator's acknowledgement that it requires it to think about how to attract international businesses to the UK and enable UK-based firms to compete effectively in international markets. In advancing the SICGO, we would like to see the FCA prioritise changes that address:

- Complex and burdensome regulation that is costly and time-consuming to implement and maintain compliance systems for, particularly for smaller firms and where there is limited identifiable benefit for investors.

- Slow authorisation and approval processes. While there have already been some improvements (e.g. turnaround times for change in control notifications are now largely resolved within the 60-day statutory limit), slow and unnecessary regulatory checks disrupt the flow of investment capital, hindering business growth and innovation.

- Uncertainty and ambiguity in rules and regulatory guidance, which can make it difficult for firms to understand the regulator's expectations and promote risk-aversion and overcompliance in some areas.

Broadly, we would like to see the FCA **develop a competitive mindset** and do more to balance oversight with flexibility to enhance proportionality, holding firms to high standards and maintaining market stability without unduly constraining market activity. It would also mean monitoring international competitor regimes, not only to respond to changes to ensure the UK regime remains effective and competitive, but also to maintain regulatory alignment where needed to preserve the UK's position as a global hub for private capital (e.g. for market access or dual regulation reasons). A more competitive mindset within the regulator will make the UK more attractive to international firms, investors and talent – which will help to drive sustainable growth of the UK economy.

We also believe that **enhanced coordination between regulators and legislators** is essential for ensuring a stable, effective and competitive regulatory system in the UK. There are several areas where better coordination between HM Treasury and the FCA would help to make improvements to the UK regulatory regime to enhance proportionality and international competitiveness. For example, there are certain areas of regulation, particularly authorisation and approval processes, where the FCA is bound by legislation to assess and do things in a way that is disproportionate in some circumstances. Better coordination on a risk-based approach would provide the FCA with greater flexibility to be more proportionate and help the FCA and HM Treasury's ability to meet shared economic and regulatory goals.

While there have been some improvements, further thought needs to be given on how to improve engagement, bring down processing times and speed up investment activity involving FCA regulated and licenced firms. **Improved operational efficiency** will enable the FCA to be more effective, responsive and make better use of its resources. The time taken to complete regulatory applications and notifications is a key consideration for investment firms when choosing where to locate and invest. Slow and unnecessary regulatory approval and notification processes can significantly impact investment activity with delays and increased costs. The FCA can quickly boost the competitiveness of the UK regime by simplifying, automating and improving operational processes and procedures in its supervisory and authorisation teams (some of which will require the legislative change discussed above).

The international competitiveness of UK financial services needs the regulators to enhance proportionality. In some areas, this will require regulators to **reevaluate past decisions to "gold-plate" EU-derived requirements and legislation**. For private capital, this will require reforms of the Investment Firm Prudential Regime (IFPR) and the Alternative Investment Fund Manager Directive (AIFMD), where the UK's implementation puts UK-based firms at a competitive disadvantage when compared to their EU counterparts. We were pleased to hear comments by FCA Chair, Ashley Alder, that the FCA will prioritise making the regime for alternative asset managers more proportionate and we look forward to the upcoming rounds of consultations to see how the FCA proposes to deliver on those promises.

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The UK's regime for **screening investments to identify any risks to national security** has similarities with EU and US rules, but the statistics suggest the UK process imposes a higher and potentially unnecessary burden on legitimate investment activity. The challenge is that comparable regimes, in jurisdictions such as the US and the EU, are less expansive and onerous than the UK approach which risks putting off investors (although the US is implementing an outbound screening regime). To ensure the UK balances the need to ensure national security with the need to boost growth, changes to the approach taken by the ISU would be welcome.

The BVCA has been heavily engaged with the Cabinet Office and relevant officials on the review of the National Security and Investment Act (NSI Act) and the industry's experience of interacting with the Investment Security Unit. Although our overall impression is that the NSI Act is broadly meeting its objectives, feedback from our members suggests that the regime does not strike the right balance between protecting national security and encouraging investment in the UK.

Without these clarifications and improvements, it is our view that the difficulties faced by private capital investors will continue and could potentially lead to the UK becoming a less competitive location for attracting investment, impacting negatively on innovation and growth. In our view, there are specific areas where small improvements could help to address these issues:

- Narrow the scope:
    - The Government should not increase the scope of certain aspects of the regime, as suggested in the previous government's Call for Evidence in 2023, and should instead look to narrow and focus it. Mandatory sectors should be refined and types of transactions (such as internal restructuring) should be removed from scope.
    - For sectors that the Government is targeting for investment (as named in the new Industrial Strategy), fast track and pre-approval processes should be incorporated for investors from countries considered allies (outside the most sensitive transactions). There should be a specific carve-out for UK domestic investors. These reforms could serve to reduce regulatory barriers to low-risk deals, thereby supporting the Government's goal of stimulating investment into the UK.
- More official guidance and communication from the ISU: Members are finding that the ISU is inconsistent in its approach and can be slow to communicate. This creates uncertainty and delay in a transaction and the risk is that it could cause the business, for example a small startup looking for venture capital investment, to collapse due to cost pressures. We would therefore advocate for a case officer to be assigned to each filing from the outset to allow parties to follow up on the progress of a notification and for any queries the parties have. We also recommend that existing guidance should be updated to clarify matters in response to queries and requests to feedback and new guidance should be created via engagement with the investor community.
- Administration issues: The ISU should aim to speed up the timing of reviews, which often run to the full 30 days. This delay can significantly impact Venture Capital firms in particular which need to invest nimbly into fast growing companies. Another way to improve the smooth-running of the ISU would be to remove the need for duplication of work, such as adding a way for repeat notifiers to pre-populate sections of the notification form.
- Improvements to the Legislation: Remove the clause in legislation related to Automatic Invalidity for failure to file under the mandatory regime. Under the mandatory regime, if a notification is not made where it should have been, there is automatic invalidity. We believe that this is legally flawed for agreements governed by laws in jurisdictions other than the UK, it is disproportionate

and should therefore be reviewed. Additional safe harbours should be included and exemptions should be included now that the regime is in place and becoming established.

The BVCA's full response to the National Security and Investment Act Call for Evidence 2023 can be found here: BVCA Feedback to the National Security and Investment Act Call for Evidence 2023.pdf

Please see our response to Question 4.12 for our recommendations on how to address key barriers to private capital firms establishing and operating in the UK.

Question 4.7: How can regulation support responsible and informed risk-taking?

A more competitive mindset would see regulators do more to balance oversight with flexibility, holding firms to high standards and maintaining stability without unduly constraining market activity. It would also mean monitoring international competitor regimes, not only to respond to changes but to maintaining regulatory alignment where needed to preserve the UK's position as a global hub (e.g. for market access reasons). A more competitive regulatory environment will make the UK more attractive to international businesses, investors and talent – which will help to drive growth.

We believe there also needs to be a change in the culture of UK DC pensions, which have historically been pushed to an extremely risk averse culture by multiple regulations, and a landscape that prioritises liquidity and low investment risk. This, in turn, has resulted in extremely low levels of DC investment in the UK's most innovative sectors, and is contributing towards the low levels of retirement savings that future generations are currently expected to have.

We note there has been a concerted effort to move away from regulations appearing to require low investment risk, and a number of initiates are being explored to better enable DC to invest for the long term. The Value for Money framework that is currently in development is a welcome step. However, we have reservations about the seemingly short-term nature of some of the metrics, the level of prescription in the proposed assessment process, and the time frames over which this is likely to take effect. We believe that Government and regulators should prioritise changes aimed at tackling this short term, risk averse culture.

Question 4.8: [For Financial Services Organisations] What are the three most important factors, ranked in order, that you consider when making an investment location decision within the UK?

BVCA data shows that:

- Over 50% of the UK businesses backed by UK private capital are based outside London and the South-East, and 90% of investee companies are SMEs.
- 80% of UK jobs backed by private capital in 2023 were outside London.
- UK-based private capital firms are more likely to invest in UK companies than non-UK firms.
- UK-based firms are twice as likely to invest outside London and the South-East than those investing in the UK from abroad.

As part of our Investment Commission work, the BVCA conducted two surveys of BVCA members looking at barriers to growth and investment in the UK.

Some of the most important factors that affect whether an investment will deliver a return are beyond the control of either investors or the businesses they invest in, but are either in the direct control of government or subject to long-term government decisions: grid connections that affect whether a new manufacturing facility can operate; transport links that affect where the workforce can be drawn from. This is separate from the question of whether public investment can "crowd in" private investment in

related sectors; it is about public infrastructure that creates overall national capacity and, in the case of transport infrastructure, especially regional capacity for businesses to attract investors.

In our BVCA member survey, we found that 42% have decided not to invest in a UK business because of a lack of public infrastructure such as transport or grid connections, 43% say that significant public investment in green energy would make it easier for them to invest in UK businesses, and 34% say that significant public investment in transport infrastructure would make it easier for them to invest in UK businesses.

Survey respondents also cited a lack of investment in the regions and in transport and other infrastructure as major barriers to investing outside London and the South East.

Although over half of the 12,000 UK businesses invested in by the private capital industry are based outside London and the South East, investment in regional businesses could be even higher with improvements to infrastructure and planning decisions.

Question 4.10: What is your assessment of the UK's ability to attract global talent to the financial services sector?

In a BVCA Survey for our Investment Commission, published earlier this year, 68% of respondents told us that a less restrictive immigration regime for global talent would make it easier for them to invest in UK businesses, and 11% have decided not to invest in a UK business because of barriers to access to global talent.

The UK is not the only country seeking to attract investment. New visa schemes elsewhere in Europe are making it easier for talent in the tech sector in particular to settle in other countries for longer periods at a lower cost. Small teams at venture capital and some growth equity firms, start-ups and SMEs often lack in-house expertise in international recruitment and immigration rules, and are forced to rely on expensive external advice: streamlining the visa application process for these firms would make it much easier to attract and retain talent in the UK.

To address barriers to attracting global talent, the BVCA recommends:

- Visa schemes for top global talent should be simplified so that investors and the companies they invest in can access the talent required to grow.

- There should be clear criteria for recruiting talent into portfolio companies, that recognise the role of venture capital and growth equity: securing a defined level of funding over a defined period should be sufficient to demonstrate that a company is looking to scale and should be able to recruit skilled overseas talent in order to grow the business.

- Members have told us that the visa process for highly specialist skills is too slow. Members who invest in new and innovative technologies compete in a small talent pool for specific skills and often lose candidates to companies working in countries where visas don't take months to obtain.

Question 4.11: What is your assessment of the UK's ability to effectively upskill and reskill domestic workers for roles in the financial services sector?

Talent is key to the UK's competitiveness as a place to do business and invest, creating and supporting jobs across the country. The UK is an attractive destination for businesses and investors thanks to its deep talent pool in financial and professional services. For private capital investors, there are two different dimensions to the access to talent question: talent within private capital investment firms, and recruitment and skills within the portfolio companies they invest in.

Within the financial services industry, the competition for talent is frequently global, and or highly technical, with very specific skills which are in high demand. While the UK is an attractive place for highly talented individuals to come to lead a business, they cannot do this without the right immigration rules. Specific visa restrictions make it difficult for the UK to attract highly talented individuals, while European visa schemes for science and tech talent are more generous in length and affordability.

The UK must also ensure opportunities in employment and investment reflect the diversity of the UK's talent pool. The Rose Review found that up to £250bn of new value could be added to the UK economy if women started and scaled new businesses at the same rate as men. Government initiatives to diversify funding and leadership in the UK investment ecosystem are essential for both equality and the economic growth opportunities they present.

The cornerstone of the UK's competitiveness as a business and investment destination lies in its talent pool, and lack of access to such entrepreneurs and innovators remains an obstacle for companies seeking to scale their business.

In a BVCA Survey for our Investment Commission, published earlier this year, skills shortages in the recruitment of their domestic workforce were identified by investors as the single biggest issue for UK businesses they invest in, and a major factor in deciding not to invest in particular UK businesses.

In our survey, 79% of respondents said UK businesses they invest in have experienced problems as a result of skills shortages in the recruitment of their domestic workforce, and 25% have decided not to invest in a UK business as a result of skills shortages in the recruitment of their domestic workforce.

These shortages will vary from sector to sector, but the people we spoke to were particularly concerned about difficulty in recruiting people with certain technical skills, from heat pump installation to the ability to use particular kinds of software. In some cases, they said they were in a position to attract people with the right skills from other sectors – for example, people who can move from real estate development to renewable energy development – but noted that those sectors were also nationally important and in need of the same skilled workers, pointing to a recruitment problem that goes beyond the needs of any specific business or investor or sector.

Support for skills training programmes that focus on particular skills gaps would make it easier for businesses to be confident that they can recruit the workers they need, and for investors to back them. Improvements in secondary education and opportunities for upskilling would help to future-proof the work force.

To support a workforce for growth the BVCA recommends:

- Simplification of visa schemes for top global talent so investors and the companies they invest in can access the talent required to grow.

- Government needs to ensure that the UK has the skills to meet the needs of global investors. The UK is a leader in tech, life sciences and financial services innovation, but all of these industries need a strong pool of people with specific STEM skills. It's vital that the UK workforce is equipped for this and that our education and training systems are set up to provide the relevant training.

- Measures to drive inclusive behaviour to ensure female founders and those from diverse backgrounds can access funding to grow and scale businesses. This should include those outlined in the Women-Led High-Growth Enterprise Taskforce Report: – Government should use its convening power to increase signatories to the Investing in Women Code. – Create regional Growth Boards that bring together groups of local public and private sector stakeholders to

deliver change in the ecosystem, using Female Founders Dashboards to monitor data in the region. – Ensure that "women-led high-growth enterprises" are truly led by women: that they hold at least one of the top three positions in the organisation and have at least 25% of founder and employee equity share

Question 4.12: What barriers do international financial services firms face in either establishing and operating in the UK, or using UK markets?

The UK is currently home to one of the largest private capital hubs in the world, second only to the USA. Part of the reason for this success is because the UK has been an ideal location for US and other global firms seeking investors and investment opportunities in Europe. This has benefited the UK economy, as private capital investment managers located and raising funds in the UK are more likely to invest in UK businesses.

Despite Brexit, the UK remains a strategic entry point to European markets, with well-established networks. However, there is now fierce competition between jurisdictions to attract private capital firms, investors, investment and talent, particularly from within the EU.

As prefaced in our response to Question 4.6, the key considerations and challenges for international firms considering locating, remaining and investing in the UK include:

1. **Access to EU (and other non-UK) investors:** 86% of capital raised by UK-based private capital fund managers in 2023 was sourced from overseas investors. EU investors accounted for 19% of funds raised and remained an important source of investment for UK private capital. As a result of Brexit, access to EU investors has become more costly and complicated. The challenges for a UK firm seeking to raise capital in the EU directly (i.e. through National Private Placement Regimes (NPPR) and without an EU affiliate entity) are significant. Establishing an affiliate entity to access EU investors has its own challenges and is a costly model for UK firms, particularly for those that are not routinely fund raising. This is a long-term threat to the international competitiveness of the UK as a private capital hub.

   The UK must maintain access to EU investors to remain attractive to international private capital firms and preserve its position as a private capital hub. The UK Government should seek ways to reduce the extra cost for UK firms in raising capital from EU investors. Specifically, we would like to see the Government:

   - Engage with EU financial services policymakers via the EU/UK regulatory co-operation forum to demonstrate openness to dialogue and promote more efficient access for UK firms to investors located within the EU Single Market. For example, by pushing for equivalence decisions on NPPR.

   - Remain open to negotiations on improved AIFMD third country passport if the occasion arises. Activation of the AIFMD third country passport in its current form would require substantial changes to be attractive for UK firms and could damage existing arrangements, such as NPPR.

   - Advocate in favour of continued ability of EU firms to delegate portfolio management to or receive investment advice from UK-based firms, as necessary.

   - Engage with global policymakers to demonstrate openness to dialogue and promote more efficient access for UK firms to investors located around the world.

2. **Operational efficiencies:** The time taken to complete regulatory approvals and notifications is a key consideration for private capital firms when choosing where to locate and invest. While we recognise the importance of maintaining robust and high standards, delay is disruptive and can be costly to investment activity, particularly where speed to market is critical.

   While we recognise the FCA has made changes to improve the speed and efficiency of some approval and notification processes, more needs to be done to enhance the reputation and attractiveness of the UK as a place to establish a private capital firm and invest. Below are some examples of existing barriers and where we think targeted changes could have a positive impact on the international competitiveness of the UK regime.

   - **New funds undermanagement and "material change" notifications:** In the UK, private capital firms are required to notify the FCA of any new alternative investment funds undermanagement and subsequently of any "material change" to any fund under management. Firms are prohibited from marketing these new funds until the FCA has processed the notification or one month has elapsed. Similarly, firms are prohibited from marketing funds subject to material changes until a one month wait period has passed. The FCA's definition of 'material change' is vague and leads to firms over-reporting changes with unnecessary submissions and a series of one-month wait periods. This puts UK managed funds at a competitive disadvantage to funds managed and marketed elsewhere and damages UK competitiveness. The FCA should apply the same approach to new alternative investment funds under management and material changes as it applies to funds marketed through the National Private Placement Regime (NPPR), i.e. the obligation should simply be to file details with no wait period. This would bring the UK into line with practice in Luxembourg and Ireland, the two main competitor fund jurisdictions in the EU.

   - **The Senior Managers & Certification Regime:** SMCR is a regulatory framework that governs how financial firms manage, supervise, and assess individuals in key roles to enhance accountability. SMCR places a significant administrative burden on UK firms and was expensive to implement and continues to be so on an ongoing basis. For example, it requires legal support for implementation, changes and training, and absorbs compliance resource that would be better focussed on areas of higher risk to the firm and its investors, e.g. financial crime. There is no equivalent to the SMCR in the EU or US and it puts a large burden on UK regulated firms. In addition, the administration and process can discourage senior and knowledgeable investment professionals best placed to lead certain businesses from taking on UK board positions. We welcome the Chancellor's announcement at Mansion House that the Certification Regime is to be abolished and replaced with something more proportionate. We would like to see similar changes to enhance proportionality in the Senior Manager approval process.

   - **Change in control notifications:** Many private capital funds invest in UK businesses which hold consumer credit or insurance intermediation licences to support their core business activities, e.g. dentists, caravan park operators and online car rental companies, etc. These licenced activities are ancillary to the main business but are required to enable them to facilitate connections between lenders (who themselves will be regulated) and consumers seeking insurance, loans and other types of consumer credit. The change of control notification process that applies when investing in these businesses is time consuming and is the same process that would apply when acquiring a controlling stake in a large bank, securities broker, or asset manager. This is disproportionate and frustrates the flow of investment capital into UK businesses. While the FCA has taken steps to reduce delays, and is now turning around most change in control applications within the 60-day statutory deadline, we recommend the process

can be simplified for low-risk applications involving credit and insurance intermediation licences by making it a 'deemed approval' notification instead of an full approval process.

- **Regulatory reporting burdens:** The supervisory reporting requirements in UK AIFMD (in particular, the reporting templates in Annex IV) are disproportionately burdensome for firms, partly because they lack tailoring to private capital and are not always suited to the specificities of the asset class. In addition, the current preparation and submission process for the AIF002 is manual and does not allow for standing qualitative items (which rarely change) to be rolled forward from submission to submission, meaning each return must be fully recompiled, often on a quarterly basis. We also question the value of these reporting requirements to the FCA given it is no longer obliged to share this information with ESMA for the purposes of EU-wide analysis. In addition, the transparency reporting requirements under UK AIFMD requires full-scope UK AIFMs to regularly report information for each non-EEA AIF they manage, even where they do not comprise UK assets and do not trade on UK markets. While this requirement carries a marginal cost for UK managers of overseas funds, it may make them less cost-competitive compared to EU managers of overseas funds.

3. **Disproportionate capital requirements and remuneration rules:** Despite promising simplification, proportionality and supporting competition with more flexible rules for smaller firms, the UK's implementation of the Investment Firm Prudential Regime (IFPR) resulted in significant increases in the capital, liquidity and remuneration requirements for private capital firms. The UK implemented IFPR in a way that it is more onerous than the EU and puts UK private capital firms at a competitive disadvantage compared to their EU counterparts. This is a significant barrier and disincentive to international firms that might be considering establishing and operating in the UK.

   - **Regulatory capital requirements:** UK private capital firms now set up as adviser/arrangers to non-UK affiliate entities (to retain market access after Brexit) and those with MiFID "top-up" permissions were previously subject to an initial capital requirement of EUR 50k. As a result of IFPR, there is no maximum limit on the capital requirements for these firms, which can now run into £millions under a new percentage of fixed overheads requirement introduced by the FCA. There is no regulatory justification for this as these firms are set up in such a way that their failure would not prejudice investors in the funds that they manage. We do not agree that it makes sense to impose regulatory capital requirements on an advisor/arranger whose sole role is to provide services to a fund manager affiliate. We recommend the FCA return to a basic regulatory capital requirement of [£50k] (or potentially a higher flat requirement of say £100k), which would help put UK firms back on a more level playing field with their EU counterparts.

   - **Remuneration rules:** IFPR introduced pay rules for private capital firms for the first time. We do not believe that they address any meaningful regulatory concern, but they do impose unnecessary costs on firms, such as the cost of maintaining malus and clawback regimes. Last year, the PRA and FCA jointly announced small banks will no longer need to include malus and clawback provisions in the bonus pay-out arrangements for key staff members. This was on the basis that maintaining malus and clawback regimes is disproportionately expensive for smaller firms, who often lack the size of Human Resource departments at larger banks. We agree and we also support the PRA's analysis that the implementation of remuneration rules as part of EU-derived prudential regimes has been costly and burdensome for some firms. While we welcome positive changes to enhance the proportionality of pay rules for small banks, private capital firms are still subject to similar malus and clawback provisions despite being smaller organisations with fewer resources.

We therefore recommend that the FCA enhance proportionality of the remuneration rules for in scope private capital firms by exempting them from the malus and clawback provisions in IFPR. This will reduce cost and burdens for firms and enhance the competitiveness of the UK as a place to establish a private capital firm and help UK firms to attract new staff.

4. **Access to domestic (UK) investors:** Access to domestic investors can be a draw to international private capital firms considering establishing and operating in the UK. However, UK institutional investors, such as pension schemes and large insurers currently invest very little in UK private capital funds. UK pension funds contribute just 2%, and insurers 0.3% of the capital raised by UK-managed funds on average. This contrasts with 30% contributed by overseas pension schemes and 7% from insurers globally. It's a similar story for retail wealth management, with many successful UK entrepreneurs currently choosing to invest their wealth through EU and US structures rather than those in the UK.

   To address this, the Government must take steps to facilitate domestic investment in UK private capital. This will enable UK pension savers and investors to benefit from higher potential returns and help to provide UK companies with access to the capital they need to grow. Greater access to greater pools of domestic investment capital will enhance the attractiveness of the UK as a place to locate a private capital firm and invest.

   - **Facilitate UK institutional investment in UK private capital:** By progressing announced pension reforms, including further consolidation of UK pension schemes. However, though scale is clearly beneficial to pension schemes' ability to invest in long term, productive investments, there are other factors that will need to be considered The Government will need to ensure that consolidation leads to better governance, expertise, and diversification across different investments. It will need to protect and increase the ability of UK pensions – particularly the Local Government Pension Scheme - to allocate capital to smaller, regional private capital funds, and ensure that scale does not restrict the ability to have impact in the regions. The consolidation proposals must ensure that the right conditions are in place to support investments that have the largest impact on growth, and must ensure a focus on increasing diversification and returns, not cutting costs.

     There are also a number of regulatory barriers that could better enable pension funds to invest. For example, the FCA's permitted links rules are a significant barrier to UK defined contribution (DC) pension scheme investment in high-performing private capital assets through unit-linked funds on life insurance platforms. Life insurance platforms play an important role in how DC pension scheme money is invested, and the permitted links rules impose undue investment restrictions on professionally managed DC pension scheme default funds. This is denying UK pension savers' access to greater diversification and higher potential returns. To facilitate investment DC investment in private capital, we recommend that the FCA should:

     - exclude defaults funds of DC schemes from the 'permitted links' rules; or
     - include certain common private capital fund structures explicitly as conditional permitted links and exempting them from the 35% cap on illiquid assets.

     These changes would lift undue restrictions on DC investment in private capital, with the potential to boost investment into growing UK businesses and increase UK pension savers' pots.

For UK insurance, Solvency II capital requirements and unit linked investment rules will need to be revised to reflect reduced risk of private capital fund investments and unlock insurance capital for long-term investment in UK growth companies.

- **Foster and encourage family offices and wealthy entrepreneurs to use UK structures:** The UK's regulatory regime in this area lags behind other jurisdictions which have made changes to facilitate retail wealth management access to private capital. For example, the EU updated its European Long-Term Investment Fund (ELTIF) vehicle in 2024 to remove minimum investment amounts for retail investors and enable ELTIFs to invest in a wider range of private market assets.

  To address this gap, we recommend targeted changes to the UK regulatory framework so that sophisticated retail investors and high net worth individuals can more easily invest in UK private capital. For example, our members often find that sophisticated and high-net-worth investors, family offices, entrepreneurs, academic endowments, executives, directors, and employees of the firm that are involved in the management of the fund must be treated as retail investors despite having suitable experience and expertise. Sensible changes to better calibrate the definition of an elective professional client for private capital would help to unlock investment capital and make the UK a more attractive place to invest for appropriately knowledgeable and experienced investors. We welcome the FCA's discussion paper considering changes to the elective categorisation and opt up rules for a professional client as part of MiFID reform and will be responding with our recommendations in due course.

  In addition, the FCA should minimise unnecessary to suitable investment by minimising friction caused by UK retail regulation, such as the Consumer Duty, as it applies to non-retail and non-UK investors, and the financial promotion rules. While the Consumer Duty is underpinned by a concept of reasonableness, it is unclear how a firm is permitted to take a proportionate approach when faced with the Duty's detailed and prescriptive rules and requirements. Clarity would minimize compliance costs incurred by firms in working through areas of regulatory uncertainty.

  We welcome the abolition of the PRIIPs regime and look forward to engaging with the FCA on a replacement Consumer Composite Investment (CCI) regime that facilitates proportionate and helpful disclosures for retail investors.

5. **The tax treatment of carried interest:** As a result of recent announcements about the tax treatment of carried interest, UK private capital fund managers will face a higher effective tax rate on carried interest, on average, than their counterparts in the US and competitor jurisdictions in the EU. The UK is also looking to expand the circumstances in which it will tax non-resident managers. These changes are likely to make it more difficult for the UK to attract or retain international talent. We continue to work with the Government on its most recent carried interest consultation to achieve an outcome for venture capital and private equity that provides certainty and stability in tax policy to encourage long-term investment.

6. **VC vehicles:** To help enhance the UK VC ecosystem, we recommend that the FCA should make changes to improve the existing regime for VC managers and fund vehicles to make the UK a more competitive place for emerging VC managers to establish funds, raise capital and invest in early-stage UK businesses. It is not necessary to introduce a new type of vehicle to achieve this. Instead, this can be achieved through changes to the Registered Venture Capital fund ("RVECA") regime, which is the UK onshored version of the EU's EuVECA.

To date, there has been low take up of RVECAs due to the regime's rigidity. Amendments should seek to remove unnecessary investment barriers and ease administrative and organisational burdens inherited from the EU regime, while maintaining high regulatory standards. Changes should:

- Make the RVECA more attractive for VC managers as a UK alternative to establishing an EU EuVECA manager.
- Remove obligations that make it less attractive to VC managers than a conventional UK sub-threshold manager.
- Create a regulatory category that is used by VC fund managers, to which future regulatory change may be either applied or adapted where appropriate in order to support UK venture and investment in early stage high growth UK companies.

Further information and detailed recommendations can be found in the BVCA response to the Review of the UK Fund Regime (pages 3-7).

Question 4.13: What opportunities should the government seek to advance through its international financial services relationships?

The UK Government should leverage its international financial services relationships to strengthen its position as a global private capital hub while ensuring its financial services sector remains competitive and aligned with evolving international standards. In order to achieve this, the Government should focus on the following:

- **Influence global standard setting:** Through collaboration with international standard-setting bodies like the International Financial Reporting Standards (IFRS) Foundation and the International Sustainability Standards Board (ISSB) to shape emerging global standards for sustainability and financial reporting. The Government should advocate for the interoperability of ISSB standards with regional frameworks like EFRAG (European Financial Reporting Advisory Group) and the EU's Corporate Sustainability Reporting Directive (CSRD) to ensure UK firms can compete globally while complying with multiple regimes.

- **Monitor and align with EU regulatory developments:** Maintain close engagement with the EU on financial regulations to monitor changes and adapt UK regulations where necessary, especially on AIFMD and MiFID where changes might be required to retain market access. The Government should seek partial alignment or equivalence where feasible to maintain access to EU markets.

- **Promote regulatory interoperability:** Through mutual recognition of financial standards between the UK and EU to reduce compliance burdens for firms operating in both markets.

The Financial Services Growth & Competitiveness Strategy will seek to identify priority growth opportunities within the sector that will support long-term sustainable growth within the sector and the wider economy. The government has provisionally identified these priority growth opportunities as:

- **Fintech: Fintech opens the door for new products and services, reaching parts of the economy not reached by traditional financial services.**
- **Sustainable finance: The transition to a net zero, climate resilient, nature positive economy, and increasing demand for sustainable financial products globally, presents a real opportunity for UK financial services firms, who have already shown significant leadership in this area, as evidenced by London being ranked number one in in the Global Green Finance Index.**

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- Capital markets (including retail investment): The depth and breadth of UK capital markets is almost unparalleled. There is an opportunity to seize more global business, and to increase retail participation in the market, to the benefit of both investors and the wider economy.
- Insurance & reinsurance markets: As the world changes and new technologies and businesses grow, this presents an opportunity for the world-leading London insurance and reinsurance markets.
- Asset management & wholesale services: The UK's asset management and wholesale banking sectors are world-leading, managing the savings of millions of people, directing capital to the UK's fastest growing sectors, and anchoring financial and professional services in the UK. Shifting demographics, the rise of private markets, and the extent of cross-border activity, provide significant growth opportunities.

Question 5.1: Do you agree with the priority opportunities that have been identified?

Yes. We would emphasise the role of private capital within the last category. The UK is already a hub for private capital, with over £20bn invested in UK companies in 2023. Private capital attracts investment from across the world, deploying it as long-term investments that back British businesses of all sizes and types. This generates jobs and supports the UK as a thriving business and investment hub that helps build a better economy for the future. Ensuring that the UK remains a world-leading destination for investment is vital to driving growth within the financial services sector and the wider economy. The to the 2.2m jobs and 6% of GDP that private capital-backed companies already contribute to

Question 5.3: What do you see as the most important ingredients for a thriving UK fintech sector in coming 10 years?

Whilst the BVCA itself does not operate within the fintech sector, many of our members invest in innovative start ups and scale ups in this space. Many tech startups work with innovative technologies, from AI to medical devices to quantum technology to fintech. It is of course right that regulators take a view on new technology to protect consumers and the wider economy, however in many cases rules have not kept pace with what is now technologically possible. This makes it much more difficult for investors to understand what their return on investment is likely to be and whether a product has a reasonable path to market, if at all.

Question 5.5: In the UK's sustainable finance framework, as set out in the Chancellor's Mansion House package, do you see barriers or gaps that would support the growth and competitiveness of the UK sustainable finance market?

The BVCA is supportive of the Government's ambition to establish itself as a global leader in sustainable finance. It is acknowledged that sustainability regulation is a key pillar to achieve this vision. However, as the Government builds on the sustainability regulatory framework, it is essential that these regulations strike a careful balance between creating value whilst also remaining interoperable with existing reporting structures.

Furthermore, the regulations should be proportionate and tailored to the needs of smaller companies, which are often inadvertently impacted by the broader regulatory requirements imposed by larger investors or holding companies. Small and Medium-Sized Enterprises (SMEs) must be protected from the burden of excessive compliance requirements.

To support with this, the Government has a role to play in helping all parts of the economy to decarbonise which can be delivered by providing clear guidance and best practice frameworks to help SMEs navigate the evolving regulatory landscape. By doing so, the regulatory environment can support the development

of a sustainable finance ecosystem that is both inclusive and comprehensive, enabling businesses of all sizes to make meaningful contributions.

The Government also needs to explore innovative approaches to incentivise the flow of capital for sustainable finance. Aligned with the ambition to be a sustainable finance leader, the Government should recognise the UK's unique potential to become a Centre for Excellence in impact investing. By scaling and mainstreaming this investment approach, there is an opportunity to strengthen the foundation for a more resilient and effective sustainable finance sector. This will help attract major investors and pension capital from both local and international markets, emphasizing impact-driven outcomes. Subsequently helping to direct essential funding to underfinanced social and environmental policy areas.

As set out in Question 4.12, we believe there is significant work to be done to attract more DC pension investment into these opportunities, given the strong sustainability commitments the sector has made and strong consensus around the need for domestic pensions to be able to invest as productively as those in other nations do. The recent reforms announced in the Chancellor's Mansion House speech are welcome, and should ensure that the necessary scale is achieved. However, we do not agree that scale alone will enable DC to invest in smaller funds and opportunities, where there is often the most scope for innovation. We welcome further consideration of what conditions can be put in place to ensure that DC pension savers can support the UK's sustainable finance goals.

As discussed in more detail in our answer to question 5.7, innovative blended finance fit for purpose for private capital is a strategic tool that can be used to incentivise the flow of private capital in net zero related projects by helping to de risk investments and addressing public funding gaps. We detail the opportunities and barriers to its approaches in our answer to question 5.7.

Additionally, there is currently a lack of sustainability expertise in the market which may result in a bottleneck at the point of capital deployment, alongside market inconsistencies. This presents a significant gap as without this expertise, the move towards a global sustainable finance market will be significantly stunted. There is an opportunity for Government to engage with professional service providers to understand how growth may be stimulated through upskilling certain employees around ESG integration, risk analysis and governance.

Question 5.6: What do you think should be the UK's priority when engaging with the global sustainable finance agenda, both bilaterally and at a multilateral level?

Given the recent outcome of the US election and the potential shift towards deregulation and reduced focus on sustainability, the UK has a unique opportunity to position itself as a global leader in sustainable finance and shape the narrative showcasing what good is and can look like. To capitalise on this, the government must clearly identify and address both opportunities and challenges, setting well-defined priorities. The private capital industry is international and invests and operates across borders and it is, therefore, essential to create tangible value, foster growth and integrate broader strategic considerations in the UK, including the evolving role of private capital in driving sustainable initiatives.

The BVCA believes that the need for global cooperation is of the utmost importance. In the UK and EU alone, we note that there are already a whole host of competing regulations, reporting standards and requirements and initiatives currently putting additional costs and pressures on the private capital industry. If these can be brought under an umbrella framework such as that proposed by the International Standard Sustainable Board (ISSB) and greater alignment can be made, we believe that there will be more clarity and consistency particularly when it comes to sustainability reporting.

A further priority should be to progress exploratory work being done to understand how different blended finance mechanisms can create opportunities for investment in the private capital market. There is a need

to incentivise capital flow into nascent green technologies. It is becoming clear that blended finance options present a promising avenue for mitigating risks associated with these investments in emerging technologies, thereby enhancing their appeal to both UK and international investors, particularly within the venture capital ecosystem.

Question 5.7: What are the opportunities and barriers for the financial services sector in developing the products and/or services necessary to facilitate investment into the net zero transition? For each opportunity, please provide an indication of the type of intervention required, for example developing guidance, or supporting the development of further capabilities.

Blended finance is a strategic tool that can attract private capital into innovative infrastructure projects, especially those achieving net-zero goals. It can also be used to facilitate co-investment. By mitigating risks and leveraging public-private partnerships, it can address funding gaps and mobilise investment in green technologies and sustainable infrastructure. However, to unlock its full potential as a financing mechanism, it needs to be accompanied by robust and consistent policy frameworks alongside enhanced stakeholder engagement to understand where the pain points exist with current mechanisms. We have detailed below some of these pain points and barriers to current approaches:

- Unclear and short-term net-zero policies create regulatory uncertainty, deterring investors by making terms unpredictable and investments less appealing.
- Higher levels of risk surrounding these investments also deter investors and without appropriate de-risking mechanisms, they remain unattractive.
- Current models often fall short for large infrastructure projects, requiring more significant and sustained investments. Furthermore, evolving technologies and market demand for bespoke mechanisms emphasise the need for flexibility in blended finance models.
- Uncertainty about future liabilities and market changes combine to make long-term investment commitments harder.
- Disproportionate reporting requirements placed on smaller, scaling companies divert critical resources and energy away from driving growth. This imbalance forces these businesses to prioritise compliance over innovation, hindering their potential to expand and compete effectively.

To effectively harness the potential of blended finance and the opportunities it can create, it is essential for the Government to establish stable net zero policies and enhance the understanding of how these mechanisms can be integrated into the private capital model. The BVCA recommends:

- In line with the Industrial Strategy's need to increase market dynamism to allow labour and capital to flow more freely towards growth-driving sectors, a detailed roadmap outlining sectoral priorities, public investments and clear policies should be implemented to build investor confidence in long-term net zero projects, reduce regulatory uncertainty and foster sustained private capital investment. This can be achieved through collaboration with the UK Transition Finance Lab, leveraging its outputs developed as part of the Transition Finance Market Review.
- Development of simpler frameworks, replicable examples and targeted knowledge building to help private markets comprehend how these approaches can be used successfully. Leveraging specialist knowledge to tailor solutions for different contexts will also improve effectiveness.

- Guidance and provision of blended tools like guarantees, first-loss capital and concessional funding to reduce risks presented by emerging green technologies. Government should further look to align financing structures with investment timelines to support with this.

Question 5.8: Are there any barriers to growth in capital markets that are not being targeted by existing government reforms? How can private and public markets be grown so that they best support UK growth?

One major barrier to growth is the lack of domestic capital investing in private capital and UK capital markets more broadly. Greater access to more capital funding is crucial to supporting our most innovative businesses to grow and in the meantime, UK pension savers are missing out on the returns generated by private capital in the UK, which pension savers in other countries currently benefit from. It also means that UK businesses miss out on a domestic source of investment, notably scale-up capital that is required for these businesses to grow and remain in the UK (listed or privately held).

We are however encouraged by the proposals set out in the Chancellor's Mansion House speech, and look forward to working with the Government over the coming months to ensure that they can maximise the potential of private capital investments, in the interests of both savers, capital markets and the wider economy.

The Pensions & Private Capital Expert Panel, convened by the BVCA, outlines a series of recommendations to the current barriers that limit UK pension scheme investment into private capital, including considerations for both industries, the regulators and Government. This includes design features as the Government develops new vehicles or schemes to facilitate investment in high growth companies, a review and amendments to the permitted links rules by the FCA and the pension industry to move away from short-term cost considerations to long term returns.

The BVCA also responded to the Government's Pensions Investment Review Call for Evidence, outlining the important role large and small private capital funds play in diversification and UK growth. We welcome the proposals to require DC schemes to be a certain size and, in particular, the strong view the Government is taking on the need to move away from an excessive focus on cost in the DC market.. However, as set out elsewhere, we do have some concerns that scale alone will not be sufficient to enable pension funds to invest in lower and mid-market funds and opportunities. We have already seen some evidence of this in the pooling that has already occurred in the LGPS in recent years, where increased scale has made minimum investment sizes too large for many fund managers. The BVCA will set out further detail on what we feel are the solutions to this in our responses to the two consultations open at the moment. However, we would welcome consideration of how both DC and LGPS can be encouraged to invest in smaller growth opportunities, and support more innovation in suitability.

The Expert Panel's interim report can be found here.

BVCA full response to the Pensions Investment Review Call for Evidence can be found here.

We have supported the listing reforms and welcome the clear commitment from the UK Government on achieving increased investment from UK pension schemes into private capital funds and UK capital markets more generally.

Question 5.12: What are the barriers to setting up and conducting business as a UK asset manager or conducting wholesale services in the UK?

In addition to the points raised in our response to Question 4.12, there are opportunities to reform AIFMD to lower barriers to entry and increase proportionality, particularly for smaller firms. Our recommendations include:

- **Increase "full scope" AIFMD threshold:** There is a distinction in AIFMD between "full scope" and "subthreshold" fund managers to recognise that the costs associated with the full application of AIFMD is disproportionate for smaller managers. However, the £500m AuM threshold has not changed since 2013. As a result, the size of firm now inside the full-scope regime is smaller in real terms than was considered appropriate when AIFMD was designed and the threshold first implemented. To address this regulatory cliff edge, which is stunting the growth of some managers, we recommend that the AuM threshold is increased to £1bn to help ensure smaller managers are protected from the regulatory obligations intended for larger firms. This will help to create a more proportionate and attractive regulatory regime in the UK in which to establish a private capital firm and help to direct essential funding to support the creation, growth, and development of entrepreneurial and innovative UK companies.

- **Increase proportionality with an 'opt-in' full scope regime:** One option that the FCA could consider to ensure the UK remains an attractive place to set up a private capital firm, is to allow firms to 'opt-in' to full scope AIFMD. This would mean that all AIFMs would be subject to the regime that currently applies to subthreshold AIFMs, unless they opt-in to the full scope regime and requirements. An alternative is to retain a mandatory version of UK AIFMD for full scope AIFMs (i.e. those exceeding an AuM threshold) but to make certain provisions opt-in only, e.g. the requirement to appoint a depositary. Either route would enable groups with regulated AIFMs in the UK and EU to continue to operate their UK AIFM and EU AIFM under similar rules. An opt-in regime would provide UK private capital firms that do not intend to raise capital in the EEA with an attractive opportunity to be subject to more proportionate rules that maintain high standards for investors and are more closely tuned to the UK and broader international markets.

- **Abolish the AIFMD business restriction:** A restriction in FCA rules prohibits AIFMs from carrying on any activities other than a narrowly defined list of non-core "MiFID top-up" activities. This serves no clear purpose (there is no equivalent restriction on other types of regulated firm) and prevents firms licensed as full-scope UK AIFMs from carrying on other types of regulated or unregulated business that are complementary to the firm's AIFM activities. In practice, this means that UK firms are required to establish multiple entities with multiple licences to be able to offer the full range of services that they wish to offer to their clients. This gives rise to significant unnecessary costs and administrative burdens and acts as a barrier to entry for smaller managers. The FCA has already recognised in its guidance that an AIFM should be permitted to carry on residual collective investment scheme operator activities. We recommend that the AIFM business restriction should be abolished entirely.

Question 5.13: In what ways could the regulatory landscape for asset management or wholesale services adapt to the needs of organisations over the next 10 years?

In addition to our responses to Questions 4.12 and 5.12, we would welcome a Long-Term Asset Fund (LTAF) review in 2025 to assess how LTAFs have influenced the investment landscape, particularly in providing retail and DC pension investors access to private market assets, including private capital funds. Based on the review findings, there should be adjustments to the rules governing the LTAF to enhance its attractiveness and alignment to policy goals, such as promoting long-term investment in UK productive assets.