Asset Management Unit
HM Treasury
1 Horse Guards Road
SW1A 2HQ

Response sent by email to: AIFMR@hmtreasury.gov.uk

25 May 2025

INREV Response to HMT consultation on future regulation of alternative fund managers (April 2025)

Dear Asset Management Team,

The European Association for Investors in Non-Listed Real Estate Vehicles[1] (INREV) welcomes the opportunity to respond to the HMT's consultation on regulations for alternative investment fund managers. We hope our attached comments will make a constructive contribution to this important topic.

If you have any questions or would like to discuss our response, please contact me at jeff.rupp@inrev.org.

Sincerely,

Jeff Rupp
Director of Public Affairs

[1] INREV is the European Association for Investors in Non-Listed Real Estate Vehicles. We provide guidance, research and information related to the development and harmonisation of professional standards, reporting guidelines and corporate governance within the non-listed property funds industry across Europe.

INREV currently has more than 500 members. Our member base includes institutional investors from around the globe including pension funds, insurance companies and sovereign wealth funds that provide critical income security for more than 172 million people, as well as investment banks, fund managers, fund-of-funds managers and advisors representing all facets of investing in non-listed real estate vehicles in the UK and the rest of Europe. Our fund manager members manage more than 500 non-listed real estate investment funds, as well as joint ventures, club deals and separate accounts for institutional investors.

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Chapter 3: Requirements for sub- threshold Alternative Investment Fund Managers

Policy Proposal to remove legislative thresholds *(3.11 – 3.12)*

1. ***Do you agree with the proposal to remove the legislative thresholds from the AIFM Regulations, enabling the FCA to determine proportionate and appropriate rules for AIFMs of all sizes?***

   In principle we agree with the proposal to remove legislative thresholds, particularly where related to the calculation of leverage. However, the success of this measure does depend on the proposals of the Financial Conduct Authority ("FCA") to bring in an appropriately proportionate regime for small AIFMs, especially in relation to internal organisation requirements, reporting obligations and the need for a depositary in a real estate context. We would strongly suggest the proportionate and appropriate regime for small AIFMs is based on the existing regime for operators of UK collective investment schemes as a starting point.

Policy Proposal for the Small Registered Regime *(3.13 – 3.26)*

2. ***Do you agree that the Small Registered Regime should be removed, as it adds significant complexity to the regulatory perimeter?***

   Yes, we agree that this regime should be removed. The process for becoming a Small Registered AIFM has materially evolved and now provides minimal benefit in terms of barriers to entry or speed to market. The creation of a more efficient, fit for purpose lower tier firm in the authorised space seems an appropriate replacement for those making the transition into the regulated arena. However, one aspect of the Small Registered Regime that was beneficial was the distinction for Property AIFMs, and we are of the view that this asset class distinction is both valid and helpful, but this should be addressed by the changes in regulation being developed by the FCA

3. ***What should we take into consideration when we review the SEF/RVECA regulations?***

   INREV has no views on this, as we represent non-listed real estate investment vehicles.

4. ***How should the Government approach the regulation of Venture Capital fund managers in future?***

   INREV has no views on this, as we represent non-listed real estate investment vehicles.

5. ***Do you agree with the proposal to require managers of unauthorised property collective investment schemes and internally managed investment companies to seek FCA authorisation?***

   Even prior to and since the introduction of AIFMD, a FCA authorised operator has been required for a UK collective investment scheme, although the operator and the small registered AIFM do not need to be the same entity. If the FCA's new regime for small AIFMs is no more onerous than the existing regime for operating a collective investment scheme, then, subject to appropriate transitional periods (see below), it would seem reasonable that small AIFMs could replace the operator and no additional burden be placed on the fund or investors.

   Closed-ended investment companies are excluded from the definition of collective investment scheme and have never required an authorised operator, although they may appoint external managers or advisers which are FCA authorised. The burden of seeking regulation for registered, internally managed investment companies is discussed below but inevitably the burden of increasing compliance or reorganising management has significant potential to reduce returns to existing investors in such vehicles and we urge caution in bringing existing, registered internally-managed vehicles within the perimeter so that any such detriment is minimised (see further below).

6. ***What would be the impact of requiring these firms to seek authorisation?***

   Firms seeking authorisation will need time and possibly capital investment to put themselves in a position to meet the organisational and regulatory capital requirements necessary for FCA authorisation. An appropriate transitional period is essential for such firms to organise themselves and undergo the authorisation process.

   HMT and the FCA should seek to ensure the proportionate regulatory regime imposed on such AIFMs does not automatically increase costs to the vehicles, and the investors in those vehicles, that they manage. A clear example would be the costs of having to appoint a depositary in circumstances where there are no custodial assets already necessitating the appointment of a custodian.

   A significant cost increase may be unavoidable for internally managed investment companies, which will be detrimental to the investors in those vehicles unless management is externalised at no additional annual cost. The necessity of such vehicles falling within the regulatory perimeter, rather than any external manager or adviser, should be reconsidered particularly if the investors are all professional investors and there is no risk of consumer detriment. If not, HM Treasury might consider a permanent exclusion for pre-existing vehicles.

Chapter 4: Policy Proposal for Listed Closed-Ended Investment Companies

Policy Proposal for regulation of managers of Listed Investment Companies *(4.5 – 4.16)*

7. ***Do you agree with the Government's proposals for the future regulation of Listed Closed-Ended Investment Companies?***

INREV has no views on this, as we represent non-listed real estate investment vehicles.

8. ***Are there any unintended consequences associated with Listed Closed-Ended Investment Companies, including those which are internally managed, being in scope of AIFM Regulation?***

   INREV has no views on this, as we represent non-listed real estate investment vehicles.

9. ***If the Government were to consider an alternative approach, such as removing certain Investment Companies from scope of the regulation, should this be limited to closed-ended investment companies listed on the London Stock Exchange, or should other types of closed-ended investment company be captured?***

   INREV has no views on this, as we represent non-listed real estate investment vehicles.

10. ***Do you consider there to be any duplication in AIFM Regulation and other regulatory requirements imposed upon Listed Closed-Ended Investment Companies, which the FCA should account for when proposing rules?***

    INREV has no views on this, as we represent non-listed real estate investment vehicles.

Chapter 5: Additional Proposals

Definitions and other perimeter issues *(5.2 – 5.7)*

11. ***Do you agree with the proposal to transfer definitions underpinning the regulatory perimeter to legislation?***

    We agree with the proposal to transfer definitional language contained in the UK AIFM Regulations 2013 and in the onshored Level 2 regulations to the Regulated Activities Order (RAO) to ensure that the RAO contains the full definitions and exclusions both from the regulated activity of managing an AIF and from the specified investment of a unit of share in an AIF.

    However, we disagree with the proposal to transfer any definitions currently contained in FCA guidance. One of the real strengths of the UK implementation of key concepts has been the very practical guidance offered by the FCA in PERG Chapter 16 on what is and what is not an AIF. Given the huge market practice that has built up applying and relying on these examples, we consider it vital that they should not be overridden in any way by moving the definitions into legislation. To that end, we note and agree with the comment in the consultation paper that HMT does not intend to change the definitions or regulatory perimeter as part of this transition, and we consider it would be most appropriate for these examples to remain as guidance in PERG.

    That being said, as a result of onshoring changes, there are some definitional gaps we have noted, and suggest these be fixed as part of this process. These include:

    - **Definition of "holding company"**: This was previously defined by Regulation 2(2)(a) of the UK AIFM Regulations 2013, by a cross-reference to the AIFMD (where it is defined in Article Art 4(1)(o)):

"*Unless otherwise defined – (a) any expression used in these Regulations which is used in the directive has the same meaning as in the directive*".

This Regulation was deleted, and now reads:

(2) Unless otherwise defined –

(a) ...

(b) any expression used in these Regulations which is used in a …EU regulation made under the directive [which forms part of [assimilated] law] has the same meaning in that regulation; and

(c) any other expression used in these Regulations which is defined for the purposes of the Act has the meaning given by the Act.

Therefore, the only place the AIFMD definition is written out in full is in PERG Chapter 16.6 (Exclusions) question 6.2 guidance. It is not the same definition as used in the FCA Glossary, which refers to the Companies Act 2006 term, and therefore we consider that the original AIFMD "holding company" definition should be incorporated into the RAO as part of this exercise.

- **Definition of "securitisation special purpose entity"**: Similarly, this term was defined by Regulation 2(2)(a) of the UK AIFM Regulations 2013, by cross referring to the definition in AIFMD (where it is in Article 4(1)(an)). PERG Chapter 16.2, qu 2.37 writes out that definition, however this was not updated when Regulation (EC) No 24/2009 of the European Central Bank was recast (by Regulation (EU) No 1075/2013 of the European Central Bank) and therefore incorporates an out-of-date description of a "securitisation". We suggest this be updated when including the definition in the RAO. We note this is not the same definition used in the FCA Glossary.

The National Private Placement Regime *(5.8 – 5.12)*

12. Do you agree with the proposal to maintain the National Private Placement Regime? Do you have any concerns with how the Regime currently operates?

We agree in principle with this proposal. The UK's NPPR process using the FCA Connect notification is straightforward and quick. It is also familiar to non-UK AIFMs, reflecting the conditions of Article 42 of the EU AIFMD for full-scope managers. HMT may want to consider whether or not it is proportionate for third country small and medium AIFMs to have to comply with all of the pre-investor requirements currently set out in FUND 3.2 and reporting requirements in FUND 3.3 and 3.4. This would also turn on how these requirements will apply to UK AIFMs following any changes: it is important that third-country AIFMs have a compliance burden that is no less onerous than that for UK AIFMs.

Marketing Notifications *(5.13 – 5.14)*

13. ***Should the requirement to notify the FCA 20 days prior to marketing be removed and what impact would this have for firms and investors?***

We agree with this proposal. It would be helpful to streamline the FCA approval process so that marketing of AIFs by full-scope AIFMs in the UK is not more onerous that for third country AIFMs under NPPR. We assume that HMT would also remove the requirement in Article 55 of the UK AIFM Regulations 2013. If there is objection to removal of the 20 day notification period, HMT should consider moving this requirement to the FCA Handbook where the FCA can provide guidance on what constitutes a material change taking an approach similar to that in SUP 15.3.27.

Private Equity Notifications *(5.15 – 5.16)*

14. ***Should the requirement for AIFMs to notify the FCA in relation to acquisition of non-listed companies, be removed or should this information be provided elsewhere?***

We agree with the proposal to remove the requirement for AIFMs to notify the FCA in those circumstances. We do not consider that there is much value in firms being required to report that information elsewhere unless the FCA will review and be able to act on that data. In our view, it is the responsibility of firms to comply with the rules applicable to them, e.g. the asset stripping rules, and the FCA would be able to assess compliance by the firms exercising its normal supervisory functions.

External Valuation *(5.17 – 5.19)*

15. ***Should the liability for external valuers be reviewed, and would any additional safeguards be required?***

We have campaigned for several years requesting that the liability for external valuers be reviewed, and (in the context of regulatory reform) have proposed additional safeguards. Hence, we very much welcome this question.

It is unfair that external valuers (appointed to UK alternative investment funds) face unlimited liability under legislation. Valuation professional bodies require valuers to hold approved Professional Liability Insurance for the work they undertake. Such insurance cannot be obtained with unlimited liability, so the current AIFM regulations effectively prevent firms that are members of and regulated by professional bodies from accepting appointments as external valuers.

No wonder that in its multi-firm review[2] of valuation processes for private market assets (published: 5th March 2025), the FCA found that it was rare for fund managers to use external valuers. The increased use of external valuers would likely assist AIFMs in addressing the risks and conflicts identified in this review.

[2] https://www.fca.org.uk/publications/multi-firm-reviews/private-market-valuation-practices#lf-chapter-id-detailed-findings-policies-procedures-and-documentation

This means that AIF investors lose out, as they are unable to benefit from valuations that are transparently external and independent from the AIFM. The reform will better allow for AIF investors to benefit from independent determinations of asset value by external valuers, with the current Regulation 24(5) [The Alternative Investment Fund Managers Regulations 2013] ("Regulation 24(5)") meaning AIF investors are placing reliance upon an AIFM's internal valuation methodologies, which runs counter to principles of investor protection and good corporate governance.

We share the view that growth in the market for external valuation services would indeed be facilitated by removing the legal liability of the external valuer.

We agree with the feedback in ConDoc paragraph 5.18 "*that this liability makes valuers cautious about taking on business and makes it challenging for them to obtain professional indemnity insurance. This particularly impacts funds investing in longer-term assets which may be more complex to value*". Such funds include funds that hold underlying real estate.

In the context of Regulation 24(5) being reformed (as we propose), there are also advantages for all UK alternative investment funds (holding investment property in the UK):

- being then aligned with the valuation benchmarks with the financial reporting requirements: both IFRS and UK GAAP implicitly encourage entities to use an independent valuer (by requiring entities to disclose if an independent, suitably qualified valuer were not used).
- it would also simplify the valuation process for UK AIFMs, as they could use the same valuations for compliance with both Accounting Standards and the UK AIFMR.

Context

Regulation 24(5) overrides any contractual limit on liability agreed between the AIFM and the valuer. This simply does not work in practice.

At present few, if any, professional valuers can or will accept appointment as external valuers by an AIFM because of the unlimited liability imposed by Regulation 24(5). Most reputable valuers in the UK are members of professional bodies that require them to have professional indemnity insurance. Moreover, some insurers will also have policy conditions that require all instructions to contain liability caps.

Proposal

We propose an amendment to Regulation 24(5) along the following lines (with amended wording in red font):

24. Valuation

(1) An external valuer must carry out the valuation function described in ***[***section 3.9 of the Investment Funds sourcebook***]*** *impartially, and with all due skill, care and diligence.*

(2) An external valuer may not delegate such valuation function to a third party.

(3) If the FCA considers the appointment of an external valuer does not comply with the implementing provisions, the FCA may require that another external valuer be appointed instead.

(4) Any liability of a full-scope UK AIFM to an AIF managed by it, or to an investor of such an AIF, arising out of the AIFM's responsibility for the proper valuation of AIF assets, the calculation of the net asset value of the AIF and the publication of that net asset value, is not affected by the appointment by the AIFM of an external valuer in respect of that AIF.

(5) (a) Where the AIFM of an AIF and the external valuer agree to limit liability of the external valuer for losses suffered by the AIFM as a result of the external valuer's negligence in performing its tasks (provided the limit of liability agreed is reasonable and proportionate to value of the AIF assets), the external valuer shall only be liable to that limit; and

(b) Subject to Regulation 24(5)(a) and irrespective of any other contractual arrangements[3]*, an external valuer is liable to the AIFM of an AIF in respect of which the external valuer is appointed for any losses suffered by the AIFM as a result of the external valuer's negligence or intentional failure to perform its tasks.*

We are aware of industry stakeholders conferring extensively with contacts at valuation firms, UK fund managers, pension funds and other institutional indirect investors and industry associations and understand from stakeholders there is widespread consensus:
1) that the proposed amendment is a workable solution; and
2) in support of the proposed amendment.

This proposal is consistent with the analysis expressed in ConDoc paragraph 5.19 (which we endorse) that: "*the external valuer would have contractual liability to the AIFM, and the AIFM would still have legal liability to the fund and its investors; the final responsibility would rest with the AIFM.*"

Explanation of proposal

From a drafting perspective, we are proposing amendments that:

- utilise existing The Alternative Investment Fund Managers Regulations 2013 Regulation 24 words and concepts; and
- are minimal in nature, so the overall Regulation 24(5) policy intent is preserved.

We hope that our proposed Regulation 24(5) amendment is self-explanatory. However, we also make the following comments:

(i) The Alternative Investment Fund Managers Regulations 2013 Regulation 24 deals with the valuation process. The Alternative Investment Fund Managers Regulations 2013 Regulation 24(4) refers to "*the AIFM's responsibility for the proper valuation of AIF assets, the calculation*

[3] Delete "*that provide otherwise*"

of the net asset value of the AIF and the publication of that net asset value". The proposed Regulation 24(5) amendment does not affect this AIFM responsibility.

(ii) Under the proposed amendment:

- If the AIFM were to:
  - appoint an external valuer; and
  - agree to limit the external valuer's liability for losses suffered by the AIFM as a result of the external valuer's negligence in performing its tasks

  then the external valuer would only be liable to that limit.

- Regulation 24(5)(b) would still provide a safeguard default option to AIFMs and external valuers who wished to use it, and this default provision would be essentially unchanged. Under the proposed amendment, however, AIFMs and external valuers would have greater flexibility than is permitted under the current legislative approach.

(iii) Industry stakeholders have suggested that - in relation to the proposed words "(*provided that the limit of liability agreed is reasonable and proportionate to value of the AIF assets*)" – it would be helpful if the Financial Conduct Authority were to consult and (in light of consultation) issue guidance on how these words may apply in practice.

EU Dimension

UK real estate funds managers can and do operate funds that service institutional and other investors from the UK and internationally, including those based in the EU. We are keen that - in respect of Regulation 24(5) and the equivalent EU AIFMD Article 19(10) - there will be alignment. The alignment may reduce barriers to capital flows from EU investors into the UK (and vice versa).

Unfortunately, the EU AIFMD II reforms[4] do not extend to EU AIFMD Article 19(10). However, in its response to the preceding review of the directive, the European Securities and Markets Authority ("ESMA") did recognise[5] that there was a problem with external valuer liability. We hope a satisfactory resolution in UK legislation may well influence future discussion in the EU potentially leading to helpful guidance from ESMA or the European Commission.

We hope that reform of Regulation 24(5) may in time prompt an equivalent reform in the EU AIFMD Article 19(10), although we recognise this will take more time.

[4] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202400927

[5] https://www.esma.europa.eu/press-news/esma-news/esma-recommends-priority-topics-in-aifmd-review

*** About INREV: the European Association for Investors in Non-Listed Real Estate Vehicles**

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