New City Initiative

Carpe Diem

Advice and Opportunities from the Boutique SME Asset Management Sector
to the Future of Financial Services

About the New City Initiative

NCI is a think tank that offers an independent, expert voice in the debate over the future of asset management..

Founded in 2010, NCI counts amongst its members some of the leading independent asset management firms in the City and the continent. The NCI gives a voice to independent, owner-managed firms that are entirely focused on and aligned with the interests of their clients and investors.

Over the last decade, a traditional "client-centric" approach has enabled entrepreneurial, owner-managed firms to emerge as an important force in a financial industry dominated by global financial giants. Now, more so than ever, these firms play a key role in preserving the stability and long-term focus of the financial sector, which is of benefit to society at large.

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Executive Summary

NCI considers the unique and considered perspective of its members, the SMEs of the asset management industry and broader financial services, in guiding a path for the future of financial services. The political and regulatory response to the Global Financial Crisis led to a focus on larger firms and the banking sector, and reforms implemented in response have sometimes led to unintended consequences, for example in the effect of liquidity regulations on the asset management sector and increased barriers to entry. Now that ten years have passed, and with the UK's focus on opportunities for the future, NCI submits that it is now the time for an alternative, bottom-up approach that draws from the wisdom and efforts of the SME sector. Drawing upon its past work, NCI shows how its members offer a distinct and important contribution to the debate about the future of financial services, concluding that any consultations and working parties must include their representatives to give the optimal outcome for the broader economy and society.

Introduction

New City Initiative (NCI) has over forty members collectively managing around £500 billion of assets and employing several thousand people. Predominantly owner-managed, NCI's members align their interests with their clients' in a transparent manner and seek to encourage competition, innovation and consumer choice in the asset management industry, within the UK and more broadly.

However, NCI's members are also productively defined otherwise: they are the Small- and Medium-Sized Enterprises (SMEs) of the asset management industry and an important cluster of such activity for the UK and global economy;[1] in acting as such, they promote innovation in the broadest sense with corollary benefits for society through economic growth, employment and global trade in services.[2]

This paper explores the lessons and opportunities that can be discerned from this vibrant and successful group of financial services businesses. It explores how governmental and regulatory focus on, and engagement with, NCI's members can provide an insightful and productive lens through which to scry and guide an auspicious future for financial services, in the UK and elsewhere.

1 New City Initiative, Start-up Britain is Here in London: Why it is Crucial to Support Financial SMEs (2011); New City Initiative, The Significance of the SME Sector in the UK Financial Services Industry (2011); New City Initiative , Boutique Asset Management: An SME Cluster (2018).
2 New City Initiative , Supporting Innovation and Entrepreneurialism in Asset Management (2017).

The Diverse Nature of Financial Services

The Shadow of the Global Financial Crisis

The Global Financial Crisis (GFC) of 2007–2009 still echoes within myriad aspects of modern society: economic components, such as financial markets, monetary and fiscal policies; psychological components, such as instability, fear and crises of authority, and; sociological components, such as social justice and the morality of the loss socialization.[3]

However, on a longer timescale and global perspective, financial crises are not uncommon.[4] What is unusual within the GFC is its origin in, and effect on, developed markets and the rapidity and global scale of effect. This included bailouts by the UK government of Northern Rock, RBS and HBOS:[5] the UK government's bailouts were mirrored by responses in Ireland, Europe and the USA.[6] This nexus has been reflected in the legal arena, such as the plethora of evolved regulations, including MiFID II and AIFMD.[7] [8]

The GFC further catalysed changes within prudential and financial supervisory regulation in the United Kingdom. In June 2012, Parliament established the Parliamentary Commission on Banking Standards (PCBS) to report on:[9] professional standards and culture in UK banking given the regulatory and competition investigations into LIBOR-setting, and; any lessons regarding corporate governance, transparency and conflicts of interest applicable to regulation or government policy.[10] The PCBS proposed a new framework including the establishment of "a Senior Persons' Regime"[11], covering specified individuals within a financial services firm, and the establishment of a set of enforceable Conduct Rules.[12]

These recommendations were implemented, leading to:[13] the creation of the Senior Managers' Regime (SMR) supervised by the Prudential Regulation Authority (PRA)

3 A G Malliaris, L Shaw and H Shefrim (eds), The Global Financial Crisis and its Aftermath: Hidden Factors in the Meltdown (Oxford University Press 2016), pp 3–24.
4 S Hsu, Financial Crises, 1929 to the Present (Second (Revised) edn, Edward Elgar 2017), pp 1–7.
5 Financial Services Authority, The Supervision of Northern Rock: A Lessons Learned Review (March 2008) (FSA Internal Audit Division, 2008); Financial Services Authority, The Failure of the Royal Bank of Scotland (December 2011) (FSA Board Report, 2011); Parliamentary Commission on Banking Standards, An Accident Waiting to Happen: The Failure of HBOS (HL Paper 144; HC 705) (Fourth Report of Session 2012-13, 2013).
6 E Grossman and C Woll, 'Saving the Banks: The Political Economy of Bailouts' (2014) 47 Comp Polit Stud 574; I H-Y Chiu, 'Comparing Directors' Duties in the Financial Services Sector with Regulatory Duties under the Senior Persons Regime - Some Critical Observations.' (2016) 27 EBLRev 261.
7 Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 ("AIFMD") OJ L 174; European Commission, European Commission Statement at the Occasion of the European Parliament Vote on the Directive on Hedge Funds and Private Equity (MEMO/10/573) (2010).
8 Directive 2014/65/EU of The European Parliament and of the Council of 15 May 2014 on Markets in Financial Instruments and amending Directive 2002/92/EC and Directive 2011/61/EU Recast ("MiFID II") OJ L 173; European Commission, More Transparent and Safer Financial Markets: European Commission welcomes European Parliament vote on updated rules for Markets in Financial Instruments (MiFID II) (STATEMENT/14/129) (2014).
9 House of Commons, 'Votes and Proceedings of 16 July 2012' No 33, p 266; House of Lords, 'Minutes of Proceedings of 17 July 2012', Item 10; D Berman, Senior Individual Accountability in the Financial Services Arena: A Practical Guide (Thompson Reuters (Professional) UK 2017), p 13.
10 Parliamentary Commission on Banking Standards, Changing Banking for Good: First Report of Session 2013-14 Volume I: Summary, and Conclusions and Recommendations (HL Paper 27-I; HC 175-I) (2013), p 8.
11 Ibid, p 34, para 97.
12 Ibid, pp 34–36, paras 97–104.
13 Financial Services (Banking Reform) Act 2013 changing Financial Services and Markets Act 2000.

and Financial Conduct Authority (FCA), and;[14] enhanced powers for the PRA and FCA including a new statutory duty for those covered by SMR to take "reasonable steps" to prevent regulatory lapse within their area of responsibility (Duty of Responsibility).[15] Initially implemented within the banking sector, SMR is to be extended to all firms regulated by the FCA, including asset managers and insurers, within 2019 as part of the wider Senior Managers and Certification Regime (SMCR).[16]

Contemporary Diversity of Financial Services

Myopia of Definitional Perception

Following from the above, there is a contemporary tendency, not least amongst legislators and their electorates, to define 'financial services' within a somewhat myopic lens, with a dual focus on banking and large size: for example, the list of global systemically important banks (G-SIBs) maintained by the Financial Stability Board (FSB).[17]

Notwithstanding the understandable focus on larger banks after the GFC, the financial services industry shows considerable diversity in business activity and organisational size: indeed, such is accepted by the planned expansion of the SMR regime to insurance and asset management. NCI submits that this narrow focus is unhelpful and now is the time to reflect upon the varied and diverse nature of the broader financial services industry. For the purposes of this paper, NCI highlights two mechanisms for differentiation: business activity, and; organisational size and structure.

Asset Management as a Distinct Activity

Asset management is a distinct activity to that undertaken by retail and investment banks, intersecting differently with the public and offering different financial and societal risk profiles. The UK asset management industry managed, at the end of 2015, £8.1 trillion, second only to the USA (£27 trillion) and constituting 37% of the European total: the UK outweighs the next three largest European countries combined.[18] These large UK assets under management include funds managed for non-UK clients, are predominantly institutional, and include specialist sectors such as hedge funds, private equity and

14 Parliamentary Commission on Banking Standards, Changing Banking for Good: First Report of Session 2013-14 Volume II: Chapters 1 to 11 and Annexes, Together with Formal Minutes (HL Paper 27-II; HC 175-II) (2013), pp 283–323.
15 Financial Conduct Authority, PS17/9: Guidance on the Duty of Responsibility: Final Amendments (including Feedback on CP16/26) to the Decision Procedure and Penalties Manual (2017); D Berman, Senior Individual Accountability in the Financial Services Arena: A Practical Guide (Thompson Reuters (Professional) UK 2017), p 14.
16 Financial Conduct Authority, CP17/25: Individual Accountability - Extending the Senior Managers and Certification Regime to all FCA firms (2017); Financial Conduct Authority, CP17/26: Individual Accountability - Extending the Senior Managers and Certification Regime to Insurers (2017).
17 Financial Stability Board, '2018 List of Global Systemically Important Banks (GSIBs)' (16 November 2018) <http://www.fsb.org/2018/11/2018-list-of-global-systemically-important-banks-g-sibs/> accessed 17 April 2019.
18 Investment Association, Asset Management in the UK 2016-2017 (September 2017) (2017).

commercial property.[19] As is developed below, elements of the asset management industry promote a longer-term mindset of patient investment and provide investors with liquidity transformation.[20]

The Importance of SMEs

Within asset management, NCI further differentiates the small- and medium-sized asset managers that constitute its members: these organisations are often manager- or partner-owned, with a distinct culture and propensity for co-operation that promotes innovation, client-focus and thoughtful risk-management practices; they choose to associate through NCI given their different needs and perspectives than the broader asset management industry.[21] Unlike very large asset managers, which can resemble the international banks in their systemic risk, NCI members share characteristics, and support needs, with the broader SME sector.[22]

The importance of SMEs to the broader economy is widely recognised: within the EU, SMEs are responsible for 99% of all businesses and 85% of all new job creation.[23] NCI submits that its members, the SMEs of the financial services industry, must likewise be acknowledged as providing the foundational underpinnings of the financial services economy.

A Distinct Message

NCI avers that asset management is a distinct activity within financial services and that, within that sub-industry, boutique SME asset management presents a distinct cohort. This separate character provides a unique perspective to the discussion about the future of the financial services industry, with commonality to the travails and vibrancy of the wider SME sector.

As such, it is submitted that government and regulators best serve their broad constituencies by recognising and listening to the perspective and proposals of NCI's members. Not only is this consistent with the policy of recognizing the importance of SMEs to the broader economy it is, by analogy, consistent with principles of broad-based consultation.[24] The remainder of this paper explores the artefacts of this unique character and culture and draws them together to provide proposals for the future direction of financial services.

19 House of Commons, Sectoral Report - Asset Management (Report for the House of Commons Committee on Exiting the European Union (21 December 2017), 2017); Investment Association, Asset Management in the UK 2016-2017 (September 2017).
20 New City Initiative , The Conundrum of Liquidity Regulation: Observations from the Boutique SME Asset Manager (2018).
21 New City Initiative , Alignment of Interest: How Culture Defines Boutiques (2017); New City Initiative , Boutique Asset Management: An SME Cluster.
22 Financial Stability Board, Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities (2017).
23 'COSME: Europe's Programme for Small and Medium-Sized Enterprises' (European Commission) <http://ec.europa.eu/growth/smes/cosme/> accessed 11 February 2018.
24 Cabinet Office, Consultation Principles 2018 (2018).

The Unique Perspective of Boutique SME Asset Managers

Alignment of Interest, Culture and Performance

NCI has previously theorised, and empirically analysed, how the structure of the boutique active asset management industry has led the development of a unique organisational culture:[25] the firm size, investment processes, owner-managed foundations, alignment of incentives and other characteristics support cultural development in a manner that is not possible for larger active asset managers and impossible, given the absence of discretion, by passive managers. NCI extended this work to propose a transmission mechanism through the firm to the fund, giving superior performance to investors: the proposed transmission mechanism is correlated to the degree of active management and co-investment, the natural competitive advantages of NCI's SME members. As such, NCI suggests that its submissions are singularly grounded in genuine alignment with investors and their outcomes.

Liquidity Transformation

One trend since the GFC has been that of regulatory-driven deleveraging of bank balance sheets through prudential regulation to implement BASEL III.[26] As NCI has noted, these regulatory initiatives have operated in absolute terms, reducing liquidity provision, and catalysed changes in market structure, for example through the development of 'shadow banking'.[27] This curtailment of bank liquidity has, directly and indirectly, changed the manner of operation of investment funds since the operation of such funds requires access to bridge liquidity to allow redemptions.

Asset managers engage in liquidity transformation: cash subscriptions are converted into assets that underlie the investment strategy and are converted back to cash to allow redemption. The degree of liquidity transformation depends on the underlying strategy and on market conditions: a real estate fund, for example, is less liquid than one in blue-chip US stocks and market liquidity is reduced in times of crisis. Especially given the degree of disclosure required, investors understand this liquidity transformation and its contribution to return by way of asset nature and redemption policy:[28] such is yet more the case when the investor is institutional.

Curtailment of bank liquidity has transferred liquidity risk from the banking sector to the asset management sector and hence to investors. Whereas the fund could historically borrow to permit redemptions, often using the assets as security, a liquidity buffer and other 'liquidity tools' are now required that directly affect the return profile for the investor.[29]

25 New City Initiative , Alignment of Interest: How Culture Defines Boutiques.
26 Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC ("CRD IV") OJ L 176/338.
27 G Wehinger, 'Bank Deleveraging, the Move from Bank to Market-Based Financing, and SME Financing' (2012) 1 OECD Journal: Financial Market Trends; New City Initiative , The Conundrum of Liquidity Regulation: Observations from the Boutique SME Asset Manager.
28 AIFMD.
29 Financial Conduct Authority, Illiquid Assets and Open-Ended Investment Funds (DP17/1) (2017), Annex 2.

As a corollary, these structural changes limit the ability of asset managers to provide counter-cyclical liquidity in times of crisis, the essence of an active mandate, hence exacerbating liquidity events. The liquidity risk has not disappeared but is transformed and falls upon the asset management sector; it is activity-based rather than entity-based: NCI has noted that this does not benefit investors.[30]

The interconnectedness of different parts of the financial services industry means that policy imposed on one segment propagates risk to another with likely unintended consequences. Any broad policy framework must be designed with input from all industry components, including the boutique SME asset management sector.

Broad-Based Innovation and The Power of Clustering

Innovation is often considered through the lens of technological change and hence manufacturing: the printing press, for example, or automobile. Yet such a focus on the artefact of innovation belies the more substantive innovation in thought, religion or politics that led to this innovative technological expression.[31] NCI has considered how innovation, correctly defined, is much broader in scope:[32] it is not just a change in process, but the development of ideas and interconnectedness between existing ideas and technologies across the value chain. SMEs have considerable advantages in innovation when defined as such: lacking the resources of larger organisations they innovate project-by-project, often in a disruptive way, and such innovation is inseparable from business-model innovation.[33]

The scale and rapidity of innovation is encouraged by the network effect, geographical and otherwise, of clusters of related organisations. Mechanisms of action can include drawing skilled labour from a single pool, development of specialist suppliers, market scale by aggregation and knowledge sharing, voluntarily or by 'spillover'.[34] National and regional governments can establish frameworks that catalyse such clusters to create and sustain regional and international competitive advantage.[35] NCI has argued that its members, the SMEs of the asset management industry with strong internal and common culture, are exemplars of a cluster and that this effect leads to a higher propensity to innovate and support ancillary services such as custody, administration, professional services, law and so on.[36]

NCI's members are well placed to engage in open innovation across the value-chain from investor through to implementation, including developing standards and technology to introduce efficiency in middle- and back-office functions. Not only will such innovation

30 New City Initiative , The Conundrum of Liquidity Regulation: Observations from the Boutique SME Asset Manager.
31 P. F. Drucker, Innovation and Entrepreneurship : Practice and Principles (Rev. ed. edn, Butterworth-Heinemann 2007).
32 New City Initiative , Boutique Asset Management: An SME Cluster.
33 W Vanhaverbeke, Managing Open Innovation in SMEs (Cambridge University Press 2017).
34 H Wolman and D Hincapie, 'Clusters and Cluster-Based Development Policy' 29 Economic Development Quarterly 135.
35 JS Engel, 'Global Clusters of Innovation: Lessons from Silicon Valley' (2015) 57 California Management Review 36.
36 New City Initiative , Boutique Asset Management: An SME Cluster.

benefit consumers, through the alignment of interest considered above, it will catalyse the creation of highly-skilled jobs and new industries. SME asset managers, like other SMEs, are more likely to engage in disruptive innovation and to do so within an open ecosystem.[37] Given the resource constraints that disproportionately affect SMEs, encouragement of innovation requires fiscal and regulatory support by government beyond that in, for example, IMS II:[38] these ideas are considered further below.

Stewardship and Patient Capital

The role of 'patient capital' in catalysing broader economic growth, and innovation, has been recognised by government as important for the broader economy.[39] NCI's members naturally look to the longer-term when considering investment returns and business models.[40] For example, one member noted how they viewed themselves as "stewards" of client capital and observed that the ability to act in that way was linked to broader organisational culture, being a "visceral thing…deeply inculcated": this perspective is consistent with the cultural factors and alignment of interest discussed above. It is submitted that, if government and regulators are sincere in wishing to promote 'patient capital', the perspective of SME asset managers is core.

The discussion of liquidity risk above indicates how regulation applied to one segment or purpose can have unintended consequences that act quite differently elsewhere. This also applies to the promotion of 'patient capital' and a long-term mindset for managers and investors. NCI identifies three examples:

- Depreciation reporting required under MiFID II;[41]
- Annual Value for Money (VfM) assessment required by the FCA;[42] and
- Use of standardised methods for transaction costs.[43]

Depreciation reporting requires an automated report to the client if the value of the portfolio declines by 10% in any reporting period and at multiples of 10% thereafter. These thresholds are not linked to the asset class, a 10% decline in a highly volatile asset class being wholly different to that in a low-volatility asset such as short-duration government bonds, nor do they distinguish between client types: one client may have very different subjective thresholds than another, especially those institutional clients which manage their portfolio exposure at an aggregated level. NCI promotes transparency to clients, but

37 W Vanhaverbeke, Managing Open Innovation in SMEs (Cambridge University Press 2017); New City Initiative , Boutique Asset Management: An SME Cluster
38 New City Initiative , Boutique Asset Management: An SME Cluster; HM Treasury, The UK Investment Management Strategy II (2017).
39 HM Treasury, Patient Capital Review: Industry Panel Response (2017).
40 New City Initiative , Alignment of Interest: How Culture Defines Boutiques
41 MiFID II.
42 Financial Conduct Authority, PS18/8: Asset Management Market Study Remedy and Changes to the Handbook — Feedback and Final Rules to CP17/18 (2018).
43 Financial Conduct Authority, 'FCA Handbook' <www.handbook.fca.org.uk> accessed 7 August 2018, COBS 19.8.

such immoveable thresholds diminish client autonomy and are otiose and misconceived: a client can readily set its own reporting by means of third-party services. Moreover, the automation and rapid-timescale prevent considered and personalised communication: this can cause panic-selling when rational purchase is optimal, inconsistent with a long-term investment horizon, and exacerbation of liquidity crises and market volatility.

In a similar manner, the annual nature of the VfM assessment creates its own myopia and encourages short-termism, the very source of many of the problems with the banking sector in the GFC: the annual VfM cycle augments the short-termism inherent in quarterly corporate reporting, for example. NCI supports the transparency of information that is required for any sort of VfM assessment, but there is a degree of subjectivity in any such assessment that rightly depends on individualised circumstances and choices: for example, fee levels may be correlated to performance. Moreover, such new reporting burdens distract the asset management organisation's board members from their right focus on broader corporate governance reforms, a key focus given the extension of SMR to asset managers. A corollary issue is how costs and charges are most effectively included within the VfM assessment: the standardised methodology can lead to a wider disparity between firms and even negative costs; it does not account for natural differences based on style and asset class risk and return distributions, nor market factors such as liquidity and market micro-structure. As with the depreciation reporting, there is a circularity and unintended consequence that misdirects in relation to genuine client value over a 'patient capital' investment period.

NCI's broad position, as exemplified by these illustrations, is that legislation and regulation must be well-considered and proportionate, with a thorough understanding of secondary effects and unintended consequences: only by looking at the effect across the entire industry and considering the ultimate effect on clients and the wider economy over the long-term can the future of the industry be viably promoted.

Proportionality and Incubation in Regulation

The discussions above provide examples of the unintended effect of legislative and regulatory response. NCI has written about the unique challenges faced by SME asset managers during their foundation and initial years, noting the disproportionate effect of regulatory cost and demands in those early years.[44] Several of NCI's members opined that they would be unable to establish themselves under current regulation as the fixed initial costs of regulatory compliance would necessitate high initial assets under management, a position unlikely to occur prior to the establishment of multi-year independent audited track record.

44 New City Initiative , Supporting Innovation and Entrepreneurialism in Asset Management.

In response, NCI proposed an extension of the FCA's Project Innovate to the asset management sector.[45] This catalysed the launch of the Asset Management Authorisation Hub, a development very much appreciated by NCI and its members.[46] However, NCI maintains that the optimal position is that embryonic asset managers be subject to a graduated regulatory burden until they have reached sufficient size, which likely occurs around the same time that their independent track record is sufficiently long to attract third-party capital: a child is not held to the same standards as an adult, albeit a rigorous framework is provided during development. Such would be consistent with the 'sandbox' of Project Innovate as applied to FinTech and other applicants: various transitional thresholds could be accelerated if the nascent asset manager grew rapidly to achieve systemic risk or if it sought to access non-institutional investors; a lighter touch may be appropriate if the investors were not located within the jurisdiction.[47]

NCI notes that such evolution of the FCA's Start-up Hub would promote yet more competition in the financial services space, increasing consumer choice and supporting innovation and entrepreneurialism. Simultaneously, it would enhance the attractiveness of the UK as a jurisdiction for establishment of financial services and corollary areas.

Competitiveness and Future Opportunities for UK Financial Services

Synthesizing the conclusions above, NCI submits that the UK is well-placed for broad financial services to thrive in the future. To do so, it must draw upon the experience of the SME sector and the core competitive advantages of the UK: these competitive advantages include the UK's linguistic and common law advantages, with a reputation for historically proportionate and well-directed regulation. This reputation must be continued and the current possibility of the UK leaving the EU allows consideration of future developments and the competitive position relative to other jurisdictions that promote asset management, notably Ireland and Luxembourg.

NCI's members have previously noted the positive international view of UK regulation, the UCITS structure and the possibilities to take advantage of increased regulatory flexibility after any departure from the EU:[48] its members' clients are across the gamut of geographies. NCI suggests that advancing the UK's position optimally requires a focus on three core structural issues:

- Establishment of a series of working groups that will include the SME sector and its valuable perspective;

45 Ibid.
46 'Asset Managers and Authorisation' (Financial Conduct Authority,, 20 December 2018) <https://www.fca.org.uk/firms/asset-managers-authorisation> accessed 20 April 2019.
47 New City Initiative , Supporting Innovation and Entrepreneurialism in Asset Management.
48 New City Initiative, A New Regime for Asset Management (2017).

- Consideration of various alternative jurisdictions and their own positioning; and
- Development of a best-practice UK fund structure and regulatory environment that will achieve wide third-jurisdiction conformance and/or acceptance.

Considerable funds are managed through UCITS and AIFs established in Ireland and Luxembourg, notwithstanding that the management and source of those funds are largely from the UK, either private individuals or institutional investors. Most investors wish the fund structure to be tax transparent, paying tax as required in their jurisdiction of domicile, and for this to be achieved by means of express exemption from taxation: the perception is that the UK does not exempt such fund vehicle from taxation but rather offers comparable relief, a position that is more readily changed by a future government. Given the inherent credibility that a larger jurisdiction has, not least in terms of macro stability and the capacity to negotiate tax treaties and regulatory mutuality with Asian and American jurisdictions, consideration of making changes to encourage 'repatriation' of these 'UK funds' would catalyse the evolution of the UK financial services industry. To ensure no reticence from investors. HMRC could pre-clear such repatriations such that there is assurance of no taxable event upon redomiciliation.

Such repatriation of 'UK funds' could benefit ancillary services in the UK such as custody, compliance, legal and professional services and other support functions, playing to the UK's natural strengths in English language and common law: a multiplier effect in terms of employment that could support the UK's regional development aims as many of these services would not be located within London. Indeed, NCI's members are told that Northern Trust's establishment of a Limerick office has offered various benefits over being located solely in Dublin: similar benefits could accrue to UK regional cities or even to Northern Ireland with the appropriate incentives. Given the dynamism, propensity for innovation and cluster effect of the SME asset management sector, its active involvement in governmental or regulatory discussions is submitted to be key.

Boutique SME Asset Managers: Lessons for the Future of Financial Services

NCI welcomes the discussions relating to the future of financial services in the UK and elsewhere, including the focus of the Treasury Select Committee given the catalysis of the UK's evolving role with the EU and opportunities that flow from that evolution.[49] NCI is confident that the UK financial services industry and the asset-management sector can seize the opportunities presented by economic and political factors and that it can best do so by consultation with, and support of, the SMEs within that arena.

Given the unique nature and perspective of smaller boutique asset managers, considered above, NCI proposes the following to advance this aim, with further particularisation to be provided at the committee or working group stage:

1. Recognition of the SME asset management sector as a distinct component of the financial service industry, with different culture, investor-alignment perspectives and contributions than larger participants.

2. Participation of this SME asset management sector on any working groups, committees or similar structures established by government or regulators.

3. Focus on consumer outcomes across the value chain, noting the optimal alignment of interest between asset manager and clients.

4. Understanding of the cross-linkages between different parts of the financial services industry, the liquidity transformation that is a core part of the asset management offering and the counter-cyclical liquidity provided by boutique active asset managers.

5. Catalysis of innovation by noting that disruptive innovation tends to come from the SME sector and through the open collaboration of clusters of similar firms and by ensuring that fiscal and legislative support is open to these SMEs not just to larger firms that innovate incrementally and in more traditional ways.

6. Consistency in considering the appropriate timescale for business development and regulatory requirements, aiming to replace myopia with a true focus on long-term investing and returns to investors consistent with 'patient capital'.

7. Proportionality in any legislative or regulatory requirements to ensure that unintended consequences are minimized, thereby preventing adverse effect on the best interests of consumers.

49 Treasury Select Committee, 'Inquiry Launched into Future of UK's Financial Services Post-Brexit' (House of Commons,, 25 January 2019) <https://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news-parliament-2017/inquiry-launch-into-the-future-of-uks-financial-services-post-brexit/> accessed 17 April 2019.

8. Development of a structural framework to promote the future success of the UK financial services industry, including:

a. Required legislative and fiscal changes to encourage repatriation of 'UK funds';

b. Creation of a world-class UK funds regime that draws upon the success of UCITS; and

c. Mutual regulatory recognition and/or bilateral passporting with third-party states, including the US, Canada and the fast-growing economies of Asia and South America.

Conclusion

The economic and political environment changes, as it always has and always will. The rate of change may be greater given current externalities, but that must suggest that the requirement for consultation be implemented as widely as possible. The experienced voice of the SME sector provides a counterpoint to that of large organisations, a wisdom closer to that of the broader demos whose investment outcomes, employment opportunities and economic-wellbeing are intimately linked to that same SME sector. NCI's members are those SMEs within financial services: they welcome contribution to the debates ahead.

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