

20th October 2022

Financial Conduct Authority
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London
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Submitted via email to: cp22-14@fca.org.uk

RE: CP22/14: Broadening retail access to the long-term asset fund

BlackRock¹ is pleased to have the opportunity to respond to the CP22/14: Broadening retail access to the long-term asset fund (LTAF), issued by the Financial Conduct Authority.

We support the objectives set out by the FCA in the Consultation Paper and are **supportive of the core proposal to broaden LTAF distribution to retail investors by recategorizing LTAF units as a Restricted Mass Market Investment (RMMI)**. We agree that – with the appropriate safeguards – these changes will benefit retail investors, by granting them access to a broader range of investment strategies that are, at present, often limited to high net worth, sophisticated, or institutional investors.

That said, there are some areas where we believe the proposal requires further attention or clarification:

1. Taxation and ISA eligibility

Tax incentives will be crucial to the success of expanding LTAF distribution to retail investors. Many retail investors in the UK use Individual Savings Accounts (ISAs) as a tax efficient wrapper for their investments. The attractiveness of the LTAF to retail investors will be significantly hampered if they are not accessible via ISAs.

One barrier, as noted by the FCA, is that the LTAF's minimum 90-day notice period makes it ineligible for stocks and shares ISAs. This would effectively preclude individuals whose capacity to invest is less than or equal to the annual ISA limit from investing in LTAFs. That is, if the LTAF is not ISA eligible, it will not be a tax efficient option for those with less than £20,000 per annum to invest to do so in LTAFs, thereby excluding large class of potential investors.

Similarly, the incentive to invest in diversified investment strategies housed in LTAF structures relative to other tax-efficient investments will be determined, in part, by the annual limit for ISAs. It is notable that the Enterprise Investment Scheme offers individuals income tax relief of 30% per year on qualifying investments of up to £1,000,000 (or £2,000,000 for investments in 'Knowledge Intensive Companies'). This gives investors the potential to reduce their income tax bill by up to £300,000 per year (and up to £600,000 for investments in knowledge-intensive companies) – compared to an annual limit of £20,000 for ISAs.

We therefore recommend that the FCA, in conjunction with HM Treasury and HM Revenue and Customs, review ISA limits and eligibility requirements pertaining to regular dealing, with a view to permitting investment in LTAFs from a wide range of investors, on comparable terms to other tax-efficient investment schemes.

¹ BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers and other financial institutions, as well as individuals around the world.

2. Risk warnings and appropriateness tests

We agree with the FCA that short, clear risk warnings are of particular importance if LTAFs are to be distributed to retail investors. However, we are concerned that the FCA proposal to identify the LTAF as a “high risk” product will not accurately capture the actual risks associated with investing in LTAFs, and unnecessarily dissuade retail investors.

As the FCA note in the consultation paper, the *investment* risk of different private market strategies will vary; while early-stage investments such as venture capital or private equity often carry higher levels of investment risk, there is typically less investment risk associated with other investments such as real estate or private credit. However, this is also the case for investment strategies focused on publicly traded assets that are currently available to retail investors: the investment risk associated with emerging market equities is different to that of investment grade corporate bonds.

Liquidity risk is the most important difference between LTAF strategies and other mainstream investments or RMMIs. We therefore recommend that the proposed risk warning is changed to emphasise the long-term and illiquid nature of LTAF investments. For example: *“Assets in this fund take a long time to buy and sell...it may take several years for you to have all your invested capital returned to you”.*

Provided the above investor risk warnings are set out clearly in the updated LTAF framework, we support the proposed requirement of an appropriateness test that restricts LTAF distribution to investors who are aware of and comfortable with the long-term nature of the investments.

However, in line with earlier comments, we believe **the proposed guidance to COBS 10 Annex 3, points 3 and 5 should be updated to reflect LTAF liquidity risks and the specific investment risks and income profile of the LTAF in question.**

3. Eligibility for Non-UCITS Retail Scheme (NURS) investments

We support the FCA’s proposal to permit a NURS FAIF to invest up to 35% of assets into a single LTAF. However, many investors will access LTAFs via non-FAIF NURS, therefore **we also strongly recommend that this flexibility is also extended to NURSs.**

On a related point, as considered in the original LTAF consultation and more recently as part of the Technical Expert Group discussions, we expect a significant portion of the UK DC Scheme market to invest in LTAFs via their existing NURS and NURS FAIF platforms. Under existing rules, a NURS or NURS FAIF investing in other collective investment schemes must ensure that the target scheme’s ability to invest in other funds is restricted to 15% (per (COLL 5.6.10R(3) and 5.7.7R(2)). This restriction is indirectly shaping LTAF design, since accommodating this limit for NURS/NURS FAIF investors creates an inadvertent investment restriction on the LTAF (i.e., that the LTAF cannot invest more than 15% of its assets via other funds).

The LTAF’s in-built flexibility to invest in funds is a crucial differentiator and important for efficiencies of scale, deployment and access to strategies. Indeed, some private asset exposures need to be held via intermediate holding vehicles and fund-like structures. We note from the consultation that there has been a move to remove this restriction in relation to NURS FAIFs investing in LTAFs, but we strongly urge the FCA to ensure this point is addressed effectively and, per the point made above, that it applies to both NURS and NURS FAIFs.

In our view, **failure to address this is highly likely to inadvertently preclude a significant portion of the target market from investing in LTAFs.**

4. 10% portfolio allocation limits

We agree with the FCA that 10% of an individual investor's portfolio is a sensible limit for exposure to LTAFs and other RMMIs. However, **we would welcome further clarity on the FCA's expectations for how and where the 10% limit should be implemented and monitored.** It is operationally impractical for asset managers to ensure individual end-investors are in line with the 10% limit; distribution models mean we frequently do not have information on end-clients' entire portfolios. We therefore believe that **the 10% limit should be communicated to investors and monitored on investment platforms that distribute LTAFs.** However, an individual investor's whole portfolio may not be housed on a single investment platform: **the FCA may wish to consider incorporating the recommended 10% portfolio limit in the risk warning presented to investors.**

5. LTAF structure and tax rules

The LTAF can currently be established as a unit trust, open-ended investment company (OEIC) or an authorised contractual scheme (ACS). As outlined in [our response to the Review of the UK Funds regime](#), as these are pre-existing vehicles that have their own set of tax rules, this can bring additional complexity and tax inefficiency when looking at broadening LTAF distribution to retail investors.

The nature of investing into private asset classes, such as those which fall within the remit of the LTAF, often requires intermediate holding structures. The wide variety of legal forms and funding instruments that are common in such holding structures means that the returns received by an LTAF will commonly be a mix of dividend, interest, and capital gains. This mixture of returns creates a mixed funds issue from a tax perspective and can result in UK corporate tax being incurred by the Fund entity.

While using the ACS structure allows tax transparency to the end investor, there are some practical limitations in using an ACS for retail investors. There would be significant operational complexity in accurately classifying each underlying item of income and gains from a UK tax perspective when looking at private investments and it would be unlikely that the detailed reporting required for a UK taxable investor would be accurately or reliably produced. To reduce this operational complexity, the alternative is to use an OEIC or Unit Trust vehicle for the establishment of a retail LTAF. This would likely result in UK corporate taxation at the level of the LTAF due to the mixed funds issue and additional operational complexities for the fund itself. However, it would restrict the complex reporting requirements to the individual and simplify their receipt of returns from the fund from a tax perspective. This approach may restrict the tax efficiency of the vehicle and the overall return to the investor.

To allow for the necessary flexibility for an LTAF to hold the types of assets for which it is designed and to be able to be invested into by retail or other UK taxable investors, we recommend that the LTAF is given the ability to be established as a tax-exempt onshore fund.

We appreciate the opportunity to address and comment on the issues raised by the Consultation Paper and look forward to continuing to work with the FCA on any specific issues which may assist in the ongoing review of the LTAF Framework.

Yours faithfully,

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