Financial services sector report

Opportunities for Standards in Investment and Asset Management

A joint study from BSI and Long Finance – 2014

Prepared by Z/Yen Group for BSI

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About the Publishers

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Executive Summary

Following the publication of *Backing Market Forces: How to Make Voluntary Standards Markets Work for Financial Services Regulation* by BSI, CISI and Long Finance in November 2013, BSI asked Z/Yen Group to research opportunities for voluntary standards development in selected sectors of financial services, starting with investment and asset management (the focus of this study), and insurance.

This report provides an overview of the opportunities for standards development in the investment and asset management (I&AM) industry that emerged throughout this study, based on interactions with industry professionals and associations during workshops and informal discussions, and responses to an online questionnaire.

While voluntary standards could help to strengthen the I&AM industry in the long run and thus contribute to restoring trust, related industry efforts have generally been undermined by short-term concerns over asset gathering and revenue generation, which makes industry-wide consensus difficult to achieve. As a result, recent improvements to the way the industry operates have come through regulation (e.g. EU UCITS or AIFM) rather than being initiated by the industry itself.

Despite this, this study finds that voluntary standards could have particular value around the design of product and services, related information and processes in I&AM.

Charge disclosure and asset classification (including related criteria) were repeatedly cited as areas where product and service information standards could improve transparency and enable greater comparability between products and services.

For process standardization in areas such as investment stewardship, fund governance and responsible investment, respondents suggested that the focus should be on harmonizing and strengthening existing standards instead of creating new ones.

Strong industry support was expressed for standards on data collection and management, an area critical to internal processes, to products, to customers and in order to meet regulatory requirements.

As the findings of this study highlight, and based on industry support, the development of standards could benefit a number of areas. Z/Yen Group recommends that BSI explores the following opportunities further:

- Governance and responsible investment standards and how to effectively strengthen these.
- Charge disclosure, by engaging with the Investment Management Association (IMA) and other industry players who are committed to improving existing practices.
- Data standards, particularly around internal processes and to meet regulatory requirements.

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1. Introduction

1.1 Background and objectives

In November 2013, BSI, CISI, and Long Finance published *Backing Market Forces: How to Make Voluntary Standards Markets Work for Financial Services Regulation* following a five-month research project which explored the role of voluntary standards in financial services.

The central finding of the report was that voluntary standards markets could play a greater role in rebuilding a safer and more trusted financial services sector. Financial services are a relatively moderate user of voluntary standards compared with other commercial sectors, such as shipping or food processing. Financial services are heavily regulated and financial regulation is complex, involving different industry actors at local, national, regional (e.g. EU), and international levels. Voluntary standards could, however, play a greater role in increasing transparency and improving industry practices while encouraging competition. The report advocated a 'New Combined Approach' to regulation in financial services featuring voluntary standards where applicable.

Following the publication of the report, BSI asked Z/Yen Group to research opportunities for voluntary standards development in selected sectors of financial services, including investment and asset management (I&AM). This research project explored gaps and opportunities for standards development in the I&AM industry. To this end, Z/Yen Group engaged a cross-section of professionals from the I&AM sector and related industry associations through two workshops (see Appendix 1), informal contacts with industry professionals, and an online questionnaire (see Appendix 2).

This report provides an overview of the opportunities and priorities for standards development in the I&AM sector that have emerged throughout the project. These opportunities are not meant to be exhaustive but point to possible priorities for standards development particularly around product and services, related information, and processes.

1.2 Voluntary standards markets

A voluntary standards market is 'a commercial system in which actual and potential buyers and suppliers of products and services rely on conformity assessments'.[1] Conformity assessments are carried out against standards and can consist of self-certification, second party and third party independent verification and certification (BSI, CISI and Long Finance, 2013). Voluntary standards are typically developed on the basis of consensus of all interested parties, are subject to unrestricted open consultation and undergo systematic review to ensure their continued validity.

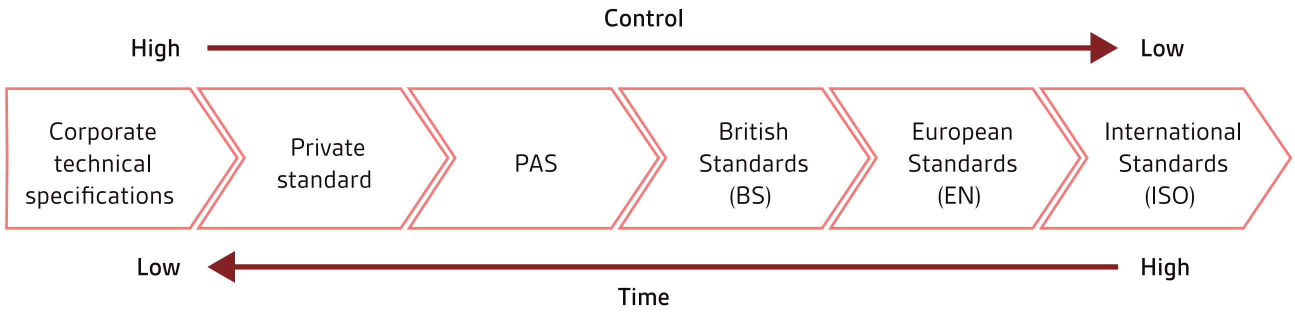
As highlighted by *Backing Market Forces* (2013), the voluntary standards markets can be categorized according to their focus, such as:

- **people standards** focus on organizational and individual behaviour, values and conduct, and include standards of professional competence and codes of conduct;
- **product standards** focus on the characteristics and technical specifications of products including design and manufacturing features, safety, interoperability and materials;
- **process standards** focus on production or operational processes and include, for example, data management, quality management systems, disclosure, reporting, risk and resilience management, and assessment standards;
- **system standards** provide rules and principles addressing risk at a systemic level including risks related to systemic stability, competition, macroprudential regulation and leverage.

Voluntary standards can evolve over time from a corporate standard – an internal specification or protocol developed and applied within an organization – to publicly available and formal standardization such as an international standard (ISO) where compliance can be independently assessed through third party verification and auditing (see Figure 1).

1 Some standards cannot be assessed but might be used as guidelines instead, for example, principle-based standards. Source: BSI, CISI and Long Finance. *Backing Market Forces* (2013), p. 2

Figure 1 — Types and evolution of standards



[Source: BSI, 2014]

Standards bring benefits by:

- reducing technical barriers to trade;
- improving risk management;
- providing a framework for achieving economies of scale, efficiencies, and interoperability;
- supporting public policy objectives; and where appropriate;
- offering effective alternatives to regulation.

Standards are market-based solutions, which enable innovation (e.g. technological standards) and support competition among industry actors where it matters and where it helps clients (e.g. standards granting market access). Competition is good insofar as it encourages innovation. Standards should not prevent desirable competition by unnecessarily restricting market access or by discouraging innovation. Competition adds value when it promotes evolution for a period of time. Standards can then emerge over time to address market needs.

2. Investment and Asset Management Industry Landscape

2.1 About investment and asset management

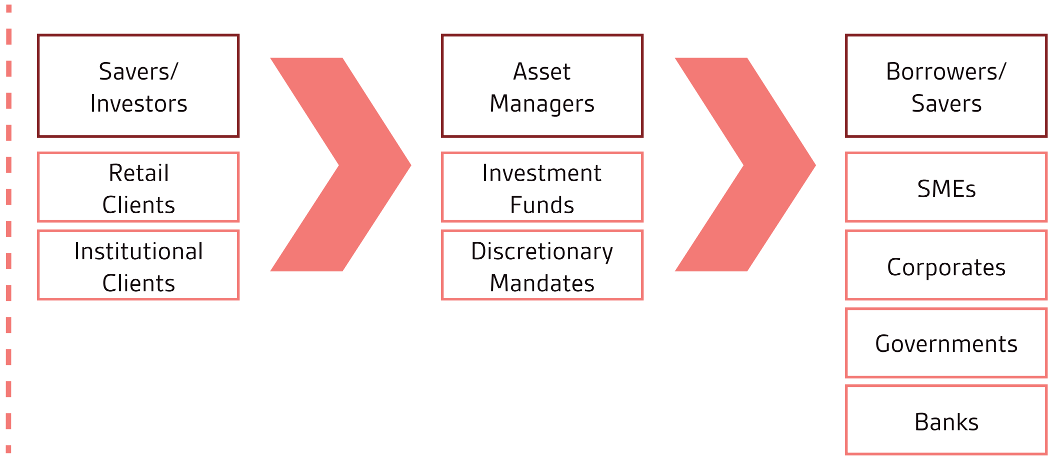
Investment and asset management (I&AM) is the professional management and trading of various securities (e.g. shares and bonds) and other types of assets (e.g. real estate) to achieve specific investment goals for the benefit of investors. Investors consist either of institutions (insurance companies, pension funds, corporations, charities, foundations, etc.) or private investors, including family offices. As shown in Figure 2, this industry plays an important role in the economy by providing a link between investors seeking appropriate savings vehicles and the financing needs of the economy (Costanzo, 2011).

Investment managers act as the 'stewards' of other people's capital, which they invest across a range of assets according to set objectives. In other words, asset managers act as 'agents' managing assets at the request of the client, in accordance with the terms of the agency agreement (Costanzo, 2011).

Asset managers develop fund products and tailor-made solutions to meet particular investment goals and objectives. Based on the Investment Management Association's (IMA) sector classification, funds can be categorized according to their principal targeted objective i.e. capital protection, income, growth or specialist and, according to the type of asset they include, for example, fixed income, equity and mixed assets (IMA n.d.).

Globally, it is estimated that the industry manages USD 87 trillion (*The Economist*, 2 August 2014). In Europe, total assets under management (AuM) amounted to EUR 16.8 trillion in 2013, with two thirds from institutional investors,

Figure 2 — Asset management in the economy



[Source: EFAMA, 2014]

in particular insurance companies and pension funds (EFAMA, 2014; Costanzo, 2011). In the UK, it is estimated that the investment management industry manages a total of GBP 5.2 trillion (IMA, n.d.).

2.2 Regulatory landscape

Similar to banking and insurance, I&AM is a tightly regulated industry at national, regional (e.g. EU) and international levels. There is a mix of solvency and investor protection regulation as well as voluntary standards. Given the concentration of insurance and pension funds, themselves highly regulated, it might be expected that a vibrant set of standards would exist. It might equally be postulated that, given the essentially simple nature of the industry, buy–hold–sell, plus the relative simplicity of the basic process, standards might unnecessarily constrain freedom-of-manoeuvre and investment capability. Since the financial crisis of 2007, all areas of finance have come under criticism. Some of the criticisms of I&AM include a lack of transparency, over-complexity, use of too many sub-parties, opaque charging structures, procyclicality of investors, over-indexing and over-selling 'active' portfolio management, and failure to reduce portfolio risks for end-investors.

In the UK, the Prudential Regulation Authority (PRA) is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. The PRA works alongside the Financial Conduct Authority (FCA) creating a 'twin peaks' regulatory structure. The FCA is responsible for promoting effective competition, ensuring that relevant markets function well, and for the conduct regulation of all financial services firms. This includes acting to prevent market abuse and ensuring that consumers get a fair deal from financial firms. The FCA conducts the prudential regulation of those financial services firms not supervised by the PRA, such as asset managers and independent financial advisers.

At the European level, the European Securities and Markets Authority (ESMA) is an independent EU authority that contributes to safeguarding the stability of the EU's financial system by ensuring the integrity, transparency, efficiency and orderly functioning of securities markets, as well as enhancing investor protection. ESMA's work on securities legislation contributes to the development of a single rulebook in Europe. In addition, ESMA develops standards such as the technical standard on the Regulation on Over-The-Counter derivatives, central counterparties and trade repositories. Three major regulatory developments with implications for the I&AM industry can be distinguished at the European level as shown in Table 1.

In the UK, the FCA has conducted thematic reviews of the asset management industry including on conflict of interests and use of commissions to pay for equity research and trading services in 2011/2012 (FSA, 2012) and more recently on anti-money laundering, anti-bribery and corruption systems and controls (FCA, 2013). This illustrates

Table 1 – EU Directives relevant to I&AM

Name	Description	Entry into force
MiFID II – Markets in Financial Instrument Directive II	Aims to increase the efficiency, transparency and resilience of European markets; includes rules to improve conditions for competition in the trading and clearing of financial instruments; to strengthen the protection of investors; and, to increase the role and supervisory powers of regulators.	Approved in 2014. Applicable from January 2017.
UCITS V – Undertakings for Collective Investment in Transferable Securities	Aims to strengthen the protection of investors with respect to UCITS funds and their depositaries.	Approved in April 2014.
AIFMD – Alternative Investment Fund Managers Directive	Requires hedge funds and private equity funds to register with national regulators; increases disclosure requirements and frequency for fund managers operating in the EU; increases capital requirements for hedge funds and places further restrictions on leverage utilized by the funds.	Applicable from July 2013.

the regulator's willingness to identify and monitor risks with the view of tightening the rules (Mansfeld, 2014). In July 2014, the Bank of England issued a Procyclicality Working Group Discussion Paper: *Procyclicality And Structural Trends In Investment Allocation By Insurance Companies And Pension Funds*. The paper pointed to the importance of life insurance companies and pension funds managing nearly GBP 3 trillion of assets in the UK, over half of the assets of the UK non-bank financial system. They explored a combination of factors that might drive the asset allocation decisions – market conventions, accounting rules and regulatory requirements – to outcomes that are suboptimal from the perspective of financial stability (through procyclicality), long-term investment, and economic growth (through an unwillingness to bear risk).

2.3 Existing standards

Many types of standards already apply to the I&AM industry. These include:

- accounting and financial reporting standards;
- international standards for securities;
- trading and business practice standards;
- information and data management standards;
- professional standards; and
- responsible investment, disclosure and reporting standards.

A quick, certainly not exhaustive, survey of existing standards follows.

Accounting and financial reporting standards include the UK GAAP, Statements of Recommended Practice (SORPs), International Valuation Standards (IVS) and IFRS 7 and 9. Accounting standards are an extremely complex, and sometimes conflicting, area with multiple national and international bodies, as well as regulators, tax authorities, and legislative oversight bodies having influence.

The International Organization of Securities Commissions (IOSCO), established in 1983, is an international body that brings together the world's securities regulators and is recognized as the global standard setter for the securities sector. IOSCO develops, implements, and promotes adherence to internationally recognized standards for securities regulation.

Internationally, the CFA Institute develops and administers codes, best practice guidelines and standards to guide the investment industry. Their Global Investment Performance Standards (GIPS) has been adopted in 37 countries, making it one of the most widely recognized voluntary standards in the industry. GIPS requires presentation of standardized statistics which have been calculated for set periods of time using prescribed methodologies and including relevant disclosures to ensure the highest level of comparability possible for clients looking to choose between different managers. Verification of compliance by 'qualified' third parties is strongly encouraged by the GIPS Executive Committee but is not yet mandatory.

BSI published PAS 55:2008, a series of standards for the management of physical assets developed with the Institute of Asset Management (IAM). PAS 55 formed the basis of a series of international (ISO) standards for Asset Management, BS ISO 55001:2014. The aim of this series of standards is to help organizations manage their assets, and the risks associated with owning them, more effectively and efficiently. Assets primarily include non-financial as well as wealth assets.

BSI publishes BS ISO 22222:2005, *Personal Financial Planning*, and BS 8577:2012, *Financial Advice and Planning Services*, standards of professional competence and ethics developed with industry and consumer bodies. Wealth management firms have adopted or been certified to the standards inside and outside of the UK using BS ISO 22222 as a core competency framework or as guidelines.

The Hedge Fund Standards Board (HFSB) was created in 2008 as a standard setting agency to address concerns and issues relevant to the hedge fund sector. It has held public consultations to strengthen standards in areas including the handling of redemptions, independent administration and governance. In 2014, the HFSB launched a new Toolbox to provide guidance to managers and investors on issues relating to fund manager governance and internal processes. The toolbox is designed to complement the Hedge Fund Standards, which managers sign up to on a comply-or-explain basis.

Responsible investment, disclosure and sustainability reporting initiatives are also relevant to the I&AM industry. The UN Principles for Responsible Investment (UN PRI) is an international network of investors working together to put six principles recognizing the materiality of environmental, social and governance issues for responsible investment into practice. Its goal is to understand the implications of sustainability for investors and support signatories to incorporate these issues into their investment decision-making and ownership practices. UNPRI counts 1260 signatories including asset owners, investment managers and service providers, accounting together for USD 45 trillion AuM.

The Global Reporting Initiative (GRI) provides all companies and organizations with a comprehensive sustainability reporting framework that is widely used around the world and which aims to improve global reporting and facilitate responsible investment. Similarly, the Sustainability Accounting Standards Board (SASB) is a non-profit organization that provides standards for disclosures, including of sustainability issues, for use by US public corporations.

TISA-sponsored PAS 156, *Specification for the Maintenance of Financial Services Customer Data* is due to publish in March 2015. The Tax Incentivised Savings Association (TISA) represents providers of pensions, ISAs and other tax efficient methods of savings for consumers. TISA members face a significant issue in maintaining contact with customers over the life time of their financial asset. Customers relocate, products are becoming more flexible and providers' back office services merge and as a result contact with customers can be lost. The new PAS aims to improve the quality of contact information to ensure customer data is accurate, regularly maintained, relevant and appropriate, and customers' financial assets are linked in providers' systems ensuring that contact with the owners of such assets is never lost. TISA believes that customer data quality can be best improved by the voluntary introduction of a quality standard supported by certification by an independent third party. This would provide customers with the assurance that their financial services provider adopts good practice in maintaining the quality of customer data and they would be unlikely to lose touch with their assets.

3. Opportunities for Standards in Investment and Asset Management

During the research carried out in 2013 (see the *Backing Market Forces* report), we gave preliminary indications of areas in financial services where voluntary standards market approaches could be suitable by contrasting the primary risk issue – people, products, processes and system – against the type of actors in financial services, using H – high, M – medium and L – low suitability. Suitability was defined as a combination of need, applicability and desire. In wholesale financial services, people and product standards were identified as highly suitable for financial advisors, while process standards were considered to have medium suitability. Standards for investors were overall perceived as less suitable for wholesale financial services. When considering retail financial services, medium suitability was found for product and process standards for banks (including investment banks), medium suitability for process standards for funds but again high suitability for people, product and process standards for advisors.

While voluntary standards could help to strengthen the I&AM industry in the long run and thus contribute to restoring trust, related industry efforts and initiatives have generally been undermined by short-term concerns over asset gathering and revenue generation, thus making industry-wide consensus difficult to achieve. As a result, recent improvements in standards for fund managers have been imposed by regulators, for example, at the European Union level with the UCITS Directive or the AIFM Directive, rather than arising from the industry itself (Mansfeld, 2014).

Voluntary standards could play a bigger role and should help to improve industry practice where benefits outweigh the costs and without reducing essential competition. Based on engagement with I&AM industry professionals, further research on opportunities for standard development in I&AM seems to confirm that voluntary standards market approaches would be particularly suitable around product and services, related information and processes.

According to respondents, people standards do not seem very relevant to the industry, except for standards intended for professional bodies and aiming to define good practice and clarify roles, for example around fiduciary duty, continuing professional development, or disciplinary procedures for members. Similarly, system standards were not found to be relevant as I&AM areas that are relevant to systemic stability are usually dealt with through regulation. Some respondents did however mention that international standards could help to improve and harmonize minimum disclosure requirements across financial jurisdictions.

3.1 Product development standards

Research showed[2] that voluntary standards could assist in optimizing product development for emerging investment opportunities such as new technologies and new asset classes, for example, digital assets.

Table 2 – Opportunities for product development standards

Area of opportunity	Description	Possible stakeholders	Potential benefits
Investment or assets related to new technologies	Improve investment risk and performance assessment through adequate framework.	• New technologies investment/fund managers • New technologies experts	• Improved understanding of risk, impact and opportunities • Optimized product development
Digital assets	Improve investment risk and performance assessment through adequate framework.	• Investment managers • Investors in digital assets • Digital assets experts	• Improved understanding of risk, impact and opportunities • Optimized product development

2 See *Backing Market Forces* (2013)

Investments or assets related to new technologies exhibit relatively higher risks due to the novelty and uncertainty surrounding the technology (e.g. alternative energy, green bonds, nanotechnology, genetically modified organisms), or difficulties underpinning the correct valuation especially for newly listed technology stocks, which often trade at high price-to-earnings multiples. Voluntary standards could help to develop adequate investment risk and performance frameworks, which in turn should help assess the performance of related investments.

Similarly, investing in and managing digital assets carries relatively higher risks including fraud. For example, the price appreciation of some cryptocurrencies (also called AltCoins) such as Bitcoin has spurred investors' interest over the past year. As funds offering investment opportunities in AltCoins emerge (DC Magnates, 2013) and given the radical novelty and high-risk nature of such investment opportunities (FINRA, 2014), there is a need for guidance and standards on how to assess related risks and performance and how to optimize product development (e.g. specific funds) and their management.

3.2 Product information standards

Voluntary standards could assist in improving the quality of information and in harmonizing disclosure practice beyond legal requirements, which in turn would be beneficial to investors in terms of understanding, transparency and satisfaction.

The classification of assets is becoming increasingly complex, particularly in relation to sustainable investments – for example is nuclear energy an 'alternative energy', 'renewable energy', 'climate-friendly', or 'unethical' investment – all are possible classifications under certain schemes. Classification standards could be examined in much more detail, in conjunction with clients who set such mandates, perhaps leading to a taxonomy of classifications of use to BSI and the industry, and helping to show where classification standards would be of use. Such standards would reduce significant information provision and exchange friction issues, for example, selling a portfolio of 'solar' financial instruments which meet a 'solar' standard facilitates trading and potentially lowers transactional costs.

Table 3 – Opportunities for product information standards

Area of opportunity	Description	Possible stakeholders	Potential benefits
Asset classification	Improve clarity and transparency on asset types and criteria for their classification.	• Investment managers and advisors, including fund managers • Investment Management Association (IMA) and other relevant industry associations	• Clarity and transparency • Greater product comparability
Charge disclosure and transparency	Improve cost transparency to allow better comparability between products and services and to determine the actual return on investment.	• Investment managers and advisors • Investors • IMA and other relevant industry associations (e.g. financial advisers)	• Investor satisfaction and understanding • Greater product comparability
Information on asset-backed securities	Better information and consistency on information and data related to securitization products across jurisdictions. Criteria to identify 'qualifying securitization'.	• Banks • Investors • Regulators (e.g. FCA)	• Transparency • Data quality • Investor satisfaction

During the course of this project, many respondents highlighted that charge disclosure – including the structure and composition of management and performance fees, the use of commissions and other related costs – was an area where standards could have a significant impact by enabling greater transparency and comparability between products and services, amidst calls from investors and greater scrutiny from policymakers and regulators (PwC, 2014). In 2012, IMA issued guidance on enhanced disclosure of fund charges and costs (IMA, 2012) and is encouraging its members to adopt the guidance and thus align their practices beyond existing legal requirements. Standards on charge disclosure seem to be an area of interest to clients (given that the nature of the I&AM sector clients are often fellow I&AM firms), to regulators, to analysts, to accountants, and to the sector itself.

Better information on product structure and backing, especially for relatively more complex products such as securitization products, was also advanced as an area where voluntary standards could help to improve transparency and thus risk assessment. The paucity of available data for some asset-based securities, for example those backed by loans to small and medium enterprises, as well as the lack of standardization of disclosure requirements across the EU were highlighted in a recent discussion paper prepared by the Bank of England and the European Central Bank. While practice is improving (e.g. ECB loan level data for ABS) and further steps are being envisaged most notably by ESMA, there is a scope for voluntary standards to support the development of disclosure frameworks for securitization products, including on their composition, asset backing, transaction documentation and performance information (Bank of England and ECB, 2014).

3.3 Process standards

Process standardization is an area in the I&AM industry where voluntary standards could have the most impact in terms of opportunities for strengthening existing standards, streamlining, efficiency gains and harmonization of procedures within and across organizations as illustrated by the number and diversity of opportunities presented in Table 4.

Investment and asset managers act as the stewards of other people's assets and capital. Codes of conduct are essential in that they provide guidance on disclosure, best practice and how managers engage with investee companies on behalf of investors. Existing codes of conduct such as the FRC's Stewardship Code in the UK (2012) are principles-based with 'comply' or 'explain' requirements. There is scope to strengthen such requirements towards a more stringent standard involving a better definition of stewardship, additional requirements in terms of disclosure and monitoring, and including second party and ultimately third party independent verification as highlighted in recent industry reports (e.g. *Standard Life* and *Tomorrow's Company*, 2014). Equally, mandates from clients often require investment and asset managers to adhere to certain investment criteria. These mandates might specify what is meant by a category such as 'metals and mining', for example, industrial metals but not gold or silver. Such mandates can also include ethical restrictions on investments such as defence, alcohol, or use of animal products. With the rise of interest in climate change and other sustainable investments, investment and asset managers have an increasing need to determine quickly whether, for example, a 'green' bond meets certain criteria, or a 'climate' bond, or a 'renewable energy' equity investment.

Voluntary standards could also play a role in improving disclosure and transparency of responsible investment policies and practices by investment and asset management firms as well as institutional investors (e.g. pension funds). Standards already exist in this area, for example the UNPRI. The industry and investors themselves are also subject to civil society scrutiny (e.g. Share Action for pensions funds in the UK) and in some instances have to comply with legal disclosure requirements (e.g. pension scheme trustees' requirement to have a Statement of Investment Principles and to include environmental, social and governance (ESG) considerations, in accordance with the UK Pensions Act as amended in 1999). Respondents suggested that there is scope to harmonize standards related to responsible investment, sustainable investment and the integration of ESG issues and improve these in terms of disclosure requirements and independent verification. While a proliferation of standards in this area might be counterproductive, working on improving an international standard from principles-based to second party verification and eventually certification and third party independent verification could be the way forward.

Similarly, fund governance, defined at its simplest as the control structure within which funds are managed, directed and controlled, is another area where respondents indicated that standards could add clarity and improve transparency. Fund governance has re-emerged as an important issue since the post-2007 financial crises and is increasingly becoming associated with fund performance, suggesting that good fund governance can support

Table 4 – Opportunities for process standards

Area of opportunity	Description	Possible stakeholders	Potential benefits
Investment stewardship	Strengthen investors' stewardship codes with more stringent requirements in terms of disclosure and verification. Relationship between asset owners and asset managers.	• IMA (and other relevant industry associations) • Institutional investors and asset owners • Fund managers	• Transparency • Benchmarking of compliance • Clarity on applicable criteria
Responsible investment (including ESG integration) policies and practices.	Improve transparency and disclosure of policies and practices related to responsible investment and the integration of environmental, social and governance issues in the investment process.	• Investment managers and funds • Institutional investors • Relevant industry associations • RI initiatives e.g. UN PRI and ShareAction	• Harmonization of requirements • Benchmarking of compliance
Fund governance structure and management	Risk-based governance structure and mechanisms.	• Fund managers • Pension funds managers • Compliance experts • Industry associations e.g. IMA • Regulators e.g. FCA	• Harmonization of requirements • Benchmarking of compliance
Investment risk management	Support the development of adequate risk management frameworks.	• Investment analysts • Industry associations e.g. IMA	• Resilience • Efficiency gains • Benchmarking of performance
Securitization	Enhancing quality, transparency, standardization of data and risk management processes across asset-based securities market.	• Risk management teams • Investment and fund managers • Investors • Regulators e.g. FCA • Industry bodies e.g. Prime Collateralised Securities Initiative (PCS)	• Transparency • Efficiency gains • Greater comparability
Better data	Data development, management, storage and distribution processes.	• Operational teams • ICT suppliers	• Data quality • Efficiency gains

capital raising objectives (e.g. for hedge funds) (KB Associates, 2013). This is a contentious assertion, but seems broadly accepted by the regulatory community. While standards do already exist, such as national corporate governance codes of conducts in Ireland and Luxembourg, these tend to lay out minimum requirements, against which compliance is disclosed on a 'comply' or 'explain' basis. Here again, there is scope to develop harmonized requirements within the EU and to strengthen these requirements for standards to evolve from a 'comply' or 'explain' standard towards second or third party independent verification.

Investment risk management has strengthened as a priority since 2007. Many firms have been re-evaluating their risk management frameworks or are currently in the process of formalizing such frameworks. Robust risk management should include:

- risk assessment, i.e. having the right tools to measure risk accurately from various perspectives;
- risk monitoring, i.e. observing the risk measures on a regular and timely basis; and
- risk-adjusted investment management (RAIM), which means using the information from the measurement and monitoring layers to ensure that the portfolio management process is aligned with expectations of risk and risk tolerance (Bender and Nielsen, 2009).

Risk management is often associated with strong governance and operational risk management. While investment and asset managers tend to have risk management policies in place, there is a broad range of acceptable risk management approaches, thus highlighting the lack of both common risk management frameworks across the industry and guidance on what constitutes best practice. Further, there is scope for modernizing existing risk assessment and management frameworks and to shift their focus from measurement to management (Stroud, 2012). Respondents suggested that voluntary standards could help by strengthening risk management frameworks, building on initial industry efforts (e.g. IWG-SWF's Santiago Principles or the Buy Side Risk Managers Forum and Capital Market Risk Advisors' Risk Principles for Asset Managers (2008)) and with the view of facilitating comparison and benchmarking across investment and asset management firms.

Data management, including the definition, collection, storage and reporting of data, was mentioned as a critical area where standards could have the most impact and help to achieve efficiencies including reducing operational costs. Data collection and management is central, whether in relation to internal processes (and these tend to vary from one financial institution to the other), to products (e.g. asset-backed securities), to customers (e.g. PAS 156 on Maintenance of customer data) or in order to streamline data transfer in standard format to meet regulatory requirements, e.g. Pensions Automatic Enrolment (PAE) in the UK.

4. Conclusion and Recommendations

4.1 Conclusion

The I&AM industry is a complex and tightly regulated industry. Opportunities for voluntary standards development exist, particularly around products and services, related information and process standards.

This research highlights that:

- **people standards** do not seem to be an important area for standards development as they are reasonably dealt with using professional bodies and training;
- **product standards** are an area for more consideration, in particular for products focusing on new asset classes and new technologies;
- **product and service information standards** were pointed out as a priority particularly around charge disclosure;
- **process standards** were an area of greater interest, particularly around stewardship, responsible investment, risk management and governance where standards could be strengthened in terms of requirements for compliance and by including verification processes. Operational and data management were also highlighted as an area for consideration, especially where standards can help to achieve efficiency gains.

4.2 Recommendations

The objective of this research was to delve deeper into one area of financial services, namely I&AM, to determine if there were more specific areas where voluntary standards markets could provide benefits. Amongst a plethora of theoretical suggestions, four areas appear worthy of further investigation based on industry interest (classification, governance, charge disclosure, and data standards), and might be useful for BSI to take forward:

- Strengthening responsible investment standards – global issue. There is potential to support and advise on efforts towards strengthening standards in two broad areas globally, classification and governance. The **classification** of assets is becoming increasingly complex, particularly for responsible investment products and assets. Classification standards could be examined in much more detail, together with clients who set such mandates, perhaps leading to a taxonomy of classifications of use to BSI and the industry, and helping to show where classification standards would be of use to add clarity and transparency. On **governance**, UN PRI has recently reviewed the way compliance with their principles was assessed, moving towards mandatory reporting, the publication of signatories' reports and independent, confidential benchmarking assessments. Governance standards are complex areas to navigate with many stakeholders, and often prompted by national or regional governments. We would suggest that organizations such as BSI largely follow those standards which gain momentum.
- **Charge disclosure** – EU focused, but with global applicability. IMA and industry players who have adopted or are preparing to implement IMA's guidance on enhanced disclosure of fund charges and costs (IMA, 2012) might find it useful to think through options to strengthen this guidance into a standard and to monitor and verify compliance.
- **Data standards** – UK focused. With CIPP PIB there is potential to provide expertise and assistance in relation to their work towards developing a free data standard to help companies meet their PAE duties.

Appendix 1: Events Held

'Voluntary Standards Markets and Investment and Asset Management'

Tuesday, 24 June 2014, 08:30 to 10:00, Z/Yen Group offices, London

This workshop invited investment and asset management professionals as well as industry association representatives to discuss the role of voluntary standards for the investment and asset management industry. The workshop attempted to address the following types of questions: What are the perceived benefits of introducing voluntary standards? What are the challenges and opportunities? Are there any existing standards that would be useful for the investment and asset management industry? Participants expressed the need for an industry-led approach to restore credibility and trust in the industry. It was felt that opportunities arose particularly around governance, products and processes.

For online information about this event

www.longfinance.net/index.php?option=com_content&view=article&id=887&Itemid=175

'Opportunities for Standards in Investment and Asset Management'

Thursday, 10 July 2014, 08:30 to 10:00, Z/Yen Group offices, London

This workshop invited investment and asset management professionals and representatives to express their opinions or views on opportunities and priorities for standards development in investment and asset management. After an overview of the first workshop and of the role and different types of standards, participants discussed several opportunities particularly around product information and processes including cost transparency, fund governance, investment stewardship, disclosure and reporting.

For online information about this event

www.longfinance.net/index.php?option=com_content&view=article&id=889&Itemid=175

Appendix 2: Questionnaire

Professionals and representatives from the industry were invited to complete a short online questionnaire. Similar questions were used during informal interviews.

1. Do you use any voluntary standards in your day-to-day role? If so, which ones?
2. To what extent do you think that the investment and asset management sector as a whole could benefit from industry-specific standards?
3. Are there any issues in the investment and asset management industry that you think are not yet addressed through regulation (either government or industry self-regulation)?
4. Which investment and asset management areas could benefit from standards development?
5. Which areas do you think should be prioritized?
6. To what extent do you think standards could be relevant in the following areas? (1 being not relevant, 3 being indifferent, 5 being very relevant.)

Areas	1	2	3	4	5
Cost transparency					
Codes of conduct					
Fund governance structures					
Investment stewardship					
Investment performance and risk assessment					
Investment performance reporting					
Investment or assets related to new technologies					
Asset/portfolio management					
ESG disclosure					
Other – please specify					

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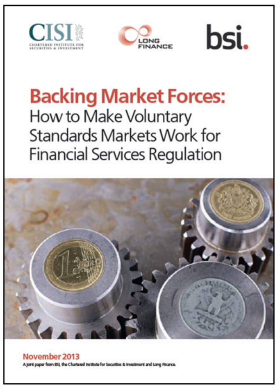
About BSI Group

BSI (British Standards Institution) is the business standards company that equips businesses with the necessary solutions to turn standards of best practice into habits of excellence. Formed in 1901, BSI was the world's first National Standards Body and a founding member of the International Organization for Standardization (ISO). Over a century later it continues to facilitate business improvement across the globe by helping its clients drive performance, manage risk and grow sustainably through the adoption of international management systems standards, many of which BSI originated. Renowned for its marks of excellence including the consumer recognized BSI Kitemark™, BSI's influence spans multiple sectors including aerospace, construction, energy, engineering, finance, healthcare, IT and retail. With over 70,000 clients in 150 countries, BSI is an organization whose standards inspire excellence across the globe.



The 2013 report *Backing Market Forces: How to Make Voluntary Standards Markets Work for Financial Services Regulation* is available at www.longfinance.net/publications.html?id=841

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