



STATE STREET

The Committee of European Securities Regulators
11-13 Avenue de Friedland
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**RESPONSE TO THE CONSULTATION ON CONTENT AND FORM OF
KEY INVESTOR INFORMATION DISCLOSURES FOR UCITS**

State Street Corporation, headquartered in Boston, U.S.A., specializes in providing institutional investors with investment servicing, investment management and investment research and trading. With \$15.1 trillion in assets under custody and \$2.0 trillion in assets under management at September 30, 2007 State Street operates in 26 countries and more than 100 markets worldwide. Our European based workforce of over 5,900 employees provides institutional investors with local support and service from our offices in Austria, Belgium, France, Germany, Ireland, Italy, the Netherlands, Switzerland, the United Kingdom, and Luxembourg.

Dear Sirs, dear Madams

State Street Corporation would like to thank CESR for the opportunity to comment on the consultation on Key Investor Information disclosures for UCITS.

We would be happy to discuss with you, in further detail, any comments you may have. Please do not hesitate to contact Gabriele Holstein at 0041 44 560 5101.

Sincerely,

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Executive Vice President
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Dr. Gabriele Holstein
Director of European Regulatory and
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**State Street Corporation’s Response to the CESR Consultation Paper on
Content and Form of Key Investor Information Disclosures
for UCITS (the “Paper”)**

INTRODUCTION

This memorandum contains State Street’s response to the Committee of European Securities Regulators (CESR) Consultation Paper on content and form of Key Investor Information (KII) disclosures for UCITS (the “Paper”). We appreciate the opportunity to share our views on this important matter. We would like to offer both general observations for CESR’s consideration, as well as responses to the specific questions raised in the Paper. We would also like to raise CESR’s attention to the fact that the SEC is currently conducting a similar consultation and that we would regard this as an opportunity for further harmonization.¹

**PART 1: BACKGROUND AND ISSUES RELATING TO KII PROPOSAL
CHAPTER 2 - SUMMARY ANALYSIS OF SP REGULATORY FAILURE**

Q1. Are respondents aware of other research which is relevant to the market and regulatory failures associated with the Simplified Prospectus (SP)?

State Street is not aware of any other research relevant to market and regulatory failures associated with the Simplified Prospectus.

When studying CESR’s summary analysis of regulatory failure, we were surprised by the statement found in paragraph 2.7. (third bullet point), that “the information investors are seeking typically is focused on investment return, along with information about risk *and costs (including fund fees, expenses and distribution costs)*”. In our view, such a statement contradicts what is found in paragraph 2.7 (first bullet point), that “(...) investors find *many key messages about charges, fund risks*

¹ Securities and Exchange Commission: Enhanced disclosure and new prospectus delivery option for registered open-end management investment companies.

and features *difficult to understand* (...).” From our experience, as well as feedback received from distributors, we are doubtful that retail investors are interested in detailed information regarding different cost components, preferring instead an all-in cost figure. Any research outcome on investor disclosure preference is strongly driven by what and how questions are posed to retail investors. In our opinion it is important to compare findings of studies which were conducted with a similar goal in mind. To illustrate our position - feedback to the question “Do you think you will still read the KII document in its entirety when additional information x,y,z would be added” is likely to yield different results than the question “What additional information is required to increase the transparency of cost associated with investing in a UCITS product”. As such, we would stress the importance of effective consumer testing via an independent organization, with clearly articulated goals and questions rather than attempts to draw conclusions based upon “other” research findings which may have only marginal relevance to the issue at hand.

Q2. Do respondents consider CESR's proposals would address the regulatory failures associated with the SP?

There is broad agreement that the Simplified Prospectus (“SP”) as currently implemented has not proven to be a useful tool to guide investors’ decisions. The Commission in its exposure draft outlined two options to enhance the effectiveness of information disclosure: “Maximum Harmonization at Level 1” (Option 1) based on a uniform “fact sheet” with the aim of developing a single document with a clearly defined set of information or “Key Investor Information” disclosures (Option 2).

We would begin by emphasizing our preference for Option 1, a point which we have raised with the Commission in previous comment requests. Should the Commission choose to implement Option 2, we believe that in order to effectively address the current failures of the SP, CESR should adopt a prescriptive approach. This is because a higher level of harmonization minimizes the risk of diverging national implementations and allows for comparability between UCITS products, two criteria which we believe to be of utmost importance. Please also refer to our response to Q7.

CHAPTER 3 - THE WIDER CONTEXT IN WHICH KII WOULD BE USED

Q3. Do respondents think that CESR has accurately described the context in which KII is likely to be used, and has correctly identified outstanding issues?

We believe that CESR has correctly identified the key outstanding issues which are not addressed by the UCITS Directive namely (i) responsibilities of UCITS operators and regulated entities involved in the operation, distribution or promotion of UCITS (ii) circumstances in which UCITS are sold within a ‘wrapper’; and (iii) interaction between the KII and other relevant Directives.

In regards to *operator and distributor responsibilities*, the draft Level 1 text articulates the responsibilities of UCITS providers when selling units directly or through a tied sales agent. We welcome CESR’s statements that where units are sold through a third party, it is the responsibility of the distributor to deliver the KII to its customers, and that the UCITS provider would fulfill its duty to make KII publicly available if it responds to requests from other regulated entities to provide them with sufficient copies. For further clarity, however, we would welcome CESR defining the terms “tied sales agent” and “sales agent”.

Furthermore, we support CESR’s view that the UCITS provider cannot legitimately be obliged to ensure that any and every potential distributor has copies of the KII. In regards to the statement that the provider would have a duty to take reasonable steps to ensure that distributors are informed when a revised version of the KII is made available, we would welcome CESR confirming that the term “reasonable steps” is to be understood in the context of a “best efforts obligation”.

In regards to *KII for UCITS packaged in a wrapper*, it is our view that the responsibility of the fund provider should be limited to the KII relating to the UCITS itself, without modification by the company responsible for the wrapper. We strongly advocate the separation of the KII from the wrapper in which it is held, as it not only benefits the end investor (transparency of extra costs associated with the use of the wrapper, enhanced comparability between the funds) but also protects UCITS

providers in the event of claims due to the underperformance of other products packaged within the wrapper.

PART II: RECOMMENDATIONS ON THE FORMAT, CONTENT AND PRESENTATION OF KII

CHAPTER 4 – GENERAL OPTIONS FOR FORMAT AND CONTENT OF KII

Recommendations on Purpose and Scope of KII

Q4. Do respondents agree with the proposed purpose and scope of KII?

We agree with CESR that the *purpose* of the KII is not (i) to be a primary marketing tool; (ii) a tool for providing regulator-to-regulator information required in the notification procedure; (iii) to be filled with legalistic disclosures; and (iv) a tool to explain all concepts used.

In regards to the *scope* of KII, we are supportive of CESR's view that KII should be produced for every UCITS fund, including those which do not promote the sale of units to the public, unless non-retail customers indicate that they do not wish to receive KII. In such cases, providers and distributors would be relieved of any obligation to deliver KII.

Q5. Should non-retail investors be permitted to opt out of receiving KII?

Referring to our response in Q4, we believe that non-retail investors should be permitted to opt out of receiving KII.

Options for the Format of the KII

Q6. Do you think that CESR's proposals on general presentation are appropriate?

We agree with CESR's proposal that the *order and hierarchy of items* to be included in the KII should be prescribed. We believe that this is essential to allow for an effective comparison between funds. Furthermore, we strongly support CESR's *plain language* proposal, whereby technical financial terms are to be avoided to the greatest extent possible.

In regards to the maximum length proposal, we would support the use of a single page format rather than a front- and back page format as suggested by CESR. Please also see our comments under Q8.

Q7. Should CESR propose adopting a more prescriptive approach, for instance using detailed templates, or should it support a less prescriptive, more principles-based approach?

We believe that CESR should adopt a more prescriptive approach – a higher level of harmonization represents a more effective basis for achieving the stated objective.

Options for the Content of the KII

Q8. In relation to the proposals on content, should Option A (with fewer items) be favored compared to option B?

We clearly support the minimal set of items (Option A)². While some of the additional items listed under Option B³, when viewed independently, might seem

² The suggested minimal set of items includes: (i) name of the fund / the management company / the promoter or group, (ii) strategy and objectives, (iii) risk/reward, (iv) past performance, (v) charges, (vi) practical information such as how to buy and sell (i.e. NAV frequency), where redemption price and other items of ongoing or specific information are available, contact details to send direct redemptions / subscriptions, distribution or capitalization of dividends, (vii) information on tax regime of the fund in its Home member state, (viii) statement on liability attached to KII, and (ix) indication of the existence of the full prospectus, where to get it / in which language it is available; (ix) identity of the competent authority, (x) date of prospectus.

³ Additional items include: (i) name of the depositary, (ii) name of the auditors, (iii) where to complain, (iv) cut-off time for dealing instructions, (v) information on the existence of other share classes, (vi) in

useful to include in the KII, it is in our view important to bear in mind that each additional piece of information incrementally dilutes the already existing information.

Furthermore, we would stress that the purpose of the KII should both reduce and simplify content compared to what currently appears in the SP. We therefore believe that *information in regards to taxes* should not be included in either Option A or Option B. This is because the cost and complexity of providing such information is likely to exceed the benefits, as (i) tax information would need to be provided for each market in which the fund is to be distributed and (ii) would need to be continuously updated to reflect changes in local law and practice.

If additional items listed under Option B are to be added, we would argue that the name of the depositary and auditors would be information both useful and easy to include.

Q9. How should both options best be tested with consumers?

For general thoughts regarding consumer testing, please see our comments made in Q1. We believe organizations specialized in this field are best placed to answer this question and as such choose not to comment.

Q10. Has CESR correctly struck the balance between reducing the information provided and ensuring investors receive the key messages they need?

Referring to our comments in Q8, we believe CESR should consider simplifying the document by withdrawing / deleting any reference to taxes, if the intention is to provide more information than a very basic statement as to how the fund is to be taxed.

case of umbrella funds - information on existence of other compartments if they are not segregated, and warning that assets of each compartment are not ring-fenced, (vii) date fund was created.

Q11. Should the competent authority of the fund and the tax regime of the fund in its Home Member State be included?

In our view, the competent authority of the fund is an easy-to-include information of potential interest to the retail investor. As stated in our comments to Q 8 and 10, tax related information should not be part of the KII.

Q12. Do you think other items of information are necessary? If so, which ones in particular?

We do not see any other items of information which are necessary.

Q13. Do you agree that distribution costs should not be systematically ‘unbundled’ within KII? Should there be flexibility to allow this where appropriate?

In our view, the question of distribution costs needs to be addressed in a wider context as it is not merely a question of KII, but of the specific distribution model used. Two different models are being applied across EU Member States today: In the case of the “bundled model” (e.g. France), investors pay an “all-in fee” with no variation between different distribution channels. The fees agreed upon between the asset management company and individual distributors are therefore not considered to be of relevance to the end-investor. In the case of the “unbundled model” (e.g. Luxembourg), costs may vary depending on the distribution channel.

A harmonization of distribution models across EU Member States could be beneficial, and should best be reviewed on the basis of a detailed study assessing the pros and cons of forcing the industry into a particular model. In the interim, there should be flexibility to allow fund providers to include a break-down of fees between the distributor and the asset manager in KII, if they wish to do so.

Local Information

Q14. Does the proposed approach of local information (a harmonized section for local information within KII, that would be precisely delineated) achieves a correct balance between the need for local information and the smooth functioning of the passport? Is a more radical approach (i.e signposting local information to a website) feasible and appropriate?

In CESR view, “local” information such as information on how to buy and sell (contact details, cut-off time, where NAV is available) should be included in KII. The section dedicated to local information however is to be very short and entirely harmonized.

We are not in agreement with CESR’s proposal and believe that the exclusion of all local information from the KII, accompanied by signposting the information on a website, would be a more feasible approach. Under current rules, there is already a requirement to provide a supplement to the prospectus detailing local information for each country. In our view, this information should not be reintroduced within the KII. Excluding local information is key in order to use the KII document cross-border, and we do not share CESR’s view that this would make the document less useful for investors and less capable of functioning as a stand-alone document.

Overall, we are concerned about CESR’s statement that the section on local information should be short and harmonized “so that no additional information could be required by the Host Member State, and that no obstacle to the notification procedure due to different domestic requirements should arise.” In our view, the statement conflicts with the purpose of KII not to be a tool for providing regulator-to-regulator information required in the notification procedure.

Use of building blocks

Q15. Should a ‘building block’ approach be permitted, whereby providers can produce different parts of the KII separately?

We do not believe that a “building block” approach should be permitted. Losing the ability to see all relevant information in a single, concise context coupled with the potential loss of comparability outweighs the flexibility available to providers and distributors to organize the information.

Fund structures – Fund of Funds, Umbrella Funds and Unit / Share Classes

Q16. Do respondents agree with the proposed treatment of funds of funds?

CESR recommends treating a fund of funds as a single fund which happens to invest in a portfolio of other collective funds. As such, the KII of a fund of funds is to be constructed with no expectation that the investor needs to be informed in detail about each of the underlying funds. We agree with CESR’s proposal. We are also in agreement with the view that for effective disclosure of risk factors and charging structure of a fund of funds, it is necessary to ‘look through’ to the characteristics of its underlying funds.

Q17. Should separate KII be produced for each sub-fund of an umbrella? Should providers be permitted to produce a compendium for all the sub-funds of an umbrella if they wish?

We agree with CESR that a separate and stand-alone KII document should be produced for each individual fund. Not only does a separate document benefit the investor by facilitating comparison between different funds, it also ensures that the fund provider is not required to update or adjust the entire document in case of changes affecting only one fund.

Q18. Do respondents agree with the proposals for treatment of unit / share classes? In particular, should providers be permitted to produce KII featuring a representative class?

According to CESR, KII requirements are to apply to every class within the UCITS. Furthermore, it is considered reasonable to (i) combine information if it does not make the KII too complex or (ii) use KII of one class on a representative basis for other classes. In the case of (ii), the following three prerequisites need to be met:

- (1) the description of risk factors should not omit any material risk applicable to any of the other classes;
- (2) where charging structures differ, the class with the highest overall charge is to be selected to represent the others;
- (3) reference is to be made to the fact that other classes are available, with an indication of where information about them can be found.

In our view, (ii) is not a reasonable approach. This is because charges and performance tend to differ strongly across UCITS classes. We share the concern that the presentation of the highest-charging class on a representative basis is likely to lead investors towards the purchase of units in that class, rather than to those with lower costs.

CHAPTER 5 – DESCRIBING THE FUND’S OBJECTIVE AND STRATEGY

Q19. Do you think that CESR’s proposals on the presentation of the strategy and objectives of a fund is appropriate?

We agree with proposed changes to the current Commission recommendation, including specific information regarding the existence of a guarantee, as well as target investors of the fund. We do not however, agree with CESR’s definition of fund objectives provided in paragraph 5.2. The objective of a fund should be defined in terms of return and not in terms of whether dividends are paid out or reinvested and/or whether capital is preserved or increased.

Q20. In particular, is it relevant to merge strategy and objectives into one generic item?

We agree with CESR’s view that the distinction between strategy and objectives is in many cases theoretical and that a joint presentation of fund strategy and objectives is to be preferred. The fund providers should, however, have some flexibility in regards to the details of how the information is to be presented.

Q21. Is the streamlining of the current applicable Recommendation relevant for the purpose of focusing the description on key elements? Do you agree with the addition of new key items to mention within that section: guarantee, period of holding inappropriate if any, design also for retail non-sophisticated investors?

Referring to our comments in Q19 and Q23, we are in agreement with CESR’s approach to streamline the current Commission recommendation and to add further information regarding a capital guarantee and type of investor, but not regarding the holding period.

Q22. More specifically, do you agree that it should be required that in case the capital is not legally guaranteed, the term ‘guaranty’ should not be used in the KII, and it should be shortly mentioned to investors how the protection is achieved ? In case the capital is legally guaranteed do you agree the guarantor should be mentioned? Do you agree that it is not necessary to mention explicitly that a fund is not capital guaranteed?

We agree with CESR that the concept of a capital guarantee needs to be carefully defined. CESR distinguishes between two types of guarantees: (i) funds offering a capital protection as a mere ‘investment objective’ which is not legally guaranteed and (ii) funds with a legal guarantee.

We agree with CESR that only funds with a so called “legal” guarantee should be allowed to use the term guarantee in the KII. The name of the guarantor, percentage of capital guaranteed, as well as terms under which the guarantee is valid, should be provided as additional information. To avoid potential confusion, funds without a legal guarantee, but offering capital protection, should state under the risk section of the KII that the fund applies certain financial techniques with the aim of providing capital protection with a brief description of how protection is to be achieved. Please also see our response to Q19 in regards to the definition of a fund objective as well as our comments in Chapter 6 on risk disclosure.

Q23. Do you agree that mentioning whether it would not be appropriate for the investor to invest into the UCITS, if he anticipates the need to redeem within a defined time period to be stated, is the appropriate way to deal with time horizon issues without leading to misunderstandings ?

The difficulty of the suggested concept is that it implies to investors that staying invested for a longer period leads to higher returns, for which there is no evidence from the academic community. We therefore do not believe that this is an appropriate way of dealing with time horizon issues. Providing the investor with a volatility estimate could be more useful.

Q24. Do you agree that giving management companies the opportunity to flag funds that have not been designed for non-sophisticated investors, with no legal consequences, would help in preventing missellings, especially in the case of ‘execution only’ subscriptions?

We do not believe that management companies should be given the opportunity to flag funds as not designed for non-sophisticated investors. Flagging bears the risk that fund providers out of a precautionary measure would potentially opt to flag all funds, making the information no longer relevant for the KII document.

CHAPTER 6 – RISK DISCLOSURE

The current risk disclosure with its plain language narrative makes it difficult for the retail investor to understand the significance of various risks. There is a tendency for providers to include all potential risks to ensure that the information can not be considered to be misleading. The significance of risk, however, is dependant on the personal circumstances of the investor as well as market conditions, both of which change over time. It is not reasonable to list all potential risks in a standard document and we share CESR’s view that this major shortcoming of the current SP needs to be addressed.

In order to address these shortcomings, CESR discusses two options: (i) **Enhancing the current pure narrative approach** without a synthetic indicator and (ii) **Implementing a synthetic risk / reward indicator** with accompanying explanatory text.

Under option 1 disclosure is to be enhanced through a number of high-level, MiFID-based principles⁴. Under Option 2 possible calculation methodologies of a synthetic

⁴ Principles to enhance pure narrative disclosure: (1) disclosure of risk/reward should enable the investor to reasonably understand the overall effect of the risk factors associated with investment in the UCITS; (2) appropriate wording should make a link between risk and reward, and make clear that there is a general correlation between possibilities of gains and possibilities of losses; (3) it should convey, in qualitative terms and based on qualitative assessment, the likelihood of loss or gain and of the size of these (...); (4) in case funds clearly target some specific markets, the risk/reward section should mention when financial techniques are used to increase or to reduce the exposure to the underlying assets. Their impact matters more than the detailed description of their functioning; (5) the wording should foster comparability between products (...); (6) the section dedicated to risk/reward presentation

risk / reward indicator are to be assessed and a common methodology to be developed at a European level, based on a draft grid of criteria provided by CESR.

According to CESR, Option 2 is the preferred solution. While option 1 has the advantage of having no methodological issues, it is not viewed to be an effective solution to address the current shortcomings of the SP. Furthermore, it is considered difficult to test the effectiveness of the principles used with consumers. The advantage of Option 2 of being an easy-to-use tool for decision making is considered to outweigh the difficulties, such as potentially complex calculation issues and the challenge of communicating the limits of the information being presented to consumers.

Before addressing the specific questions posed in the consultation paper, we would first like to share our general views on this topic. While *risk indicators* could potentially come up against the shortcomings of the current SP disclosure, we are concerned with CESR's suggestion to construct a risk / *reward* indicator for a number of reasons⁵:

First of all, future risk / return is very difficult to forecast in a way that many participants can agree. This is due to the fact that while future risk can be estimated with some degree of confidence, future return, particularly active returns, are difficult to estimate based on an agreed upon methodology. For example, historic Sharpe ratios are typically bad predictors for the future Sharpe ratio of a given product. Secondly, where return estimates are backward looking, risk / return indicators may overestimate the return and underestimate the risk if used to predict the future of active returns. Thirdly, none of the existing risk / return measures are able to capture all relevant risk factors. Last, but not least, if users focus on one number, there is likely to be commercial pressure to come up with a favorable number which may lead to a race to the bottom.

should be limited in size, (7) it should be mentioned that the risk assessment has been done taking into account only usual risks.

⁵ In the risk management practice "reward" is typically defined as "return". Please note that our comments relate to risk / return indicators as "risk / reward" indicators to our knowledge do not exist in practice.

In our view, the discussion therefore needs to focus on the key question of whether a *risk* number instead of a risk/return figure should be presented or not. This is in turn dependant on a number of issues.

Firstly, is the question of whether problems associated with trying to explain complex issues (such as limitations of any risk number) to a non-financial audience can be effectively addressed. We are concerned that consumers will become confused about the accuracy of the risk indicator which could lead to unintended consequences, including a false sense of security.

The second issue is the difficulty of developing a common methodology at the European level which can be applied to a wide range of different UCITS. For example, the time period for which the risk indicator is to be calculated may be more accurate for a certain group of UCITS but not for others, depending on how frequently the manager varies the risk level over time. Another example would be the challenge posed by differing national rules across Member States in regards to the use of derivatives.

Even if such a methodology could be agreed upon, certain flexibility is required in regards to how the computation is performed. This is due to the fact that the same risk method might not yield the same transparency across different types of funds. Asset managers should be given the opportunity to comment on the number. Referring to the first issue listed above of communicating to a non-financial audience, this bears the risk of further confusion.

The third issue is that fund providers might be tempted to calculate the numbers in such a manner that it suits the defined risk level, which questions the overall suitability of a risk indicator as key investor information.

The fourth issue we would like to raise is that it is less likely that such a risk figure can be used for comparing products against each other.

This leads us to conclude that the concept of a risk indicator is not only difficult to implement, but is laden with potential negative consequences.

Q25. Do you agree that the presentation of a synthetic indicator should be favorably tested with stakeholders and consumers?

Referring to our comments in the introduction, the concept of a risk / reward indicator should not be pursued. The key question is if a risk indicator is suited for retail clients. In our view, no consumer testing should be done by the Commission as long as this question remains open and a methodology has not been agreed upon.

Q26. What specific presentation (icon, wording, numeric scale...) should be favored, and if so on what basis?

If a risk figure is to be provided, it should in our view not be translated into a single risk scale. Please see our response to Q25 in regards to consumer testing.

Q27. How prescriptive should regulators be for the choice of a methodology, given that it should take into account largely shared risk management practices and suit investors' perception of risks?

In our view, it should not be up to the regulators, but left to the industry to agree on a methodology. In regards to the different levels of harmonization outlined by CESR, we would argue that B3 is most sensible, whereby CESR's role is limited to defining the criteria that methodologies should comply with, but would allow different compliant methodologies to co-exist.

Once there is agreement on the methodology(ies), asset managers still require flexibility in regards to how the computation is performed. In other words, regulators cannot be prescriptive in regards to the "fine tuning of a methodology" without compromising the quality and accuracy of the risk number. The managers, however, should be required to demonstrate to the relevant regulator that the numbers were calculated in a competent manner.

Q28. Are you aware of any specific existing calculation methodology that should be proposed?

If market risk is to be estimated, we believe that it should be calculated based on Value at Risk (VAR) as the common industry standard among investment banks, typically 95% - 1d-VAR. This could be calculated in different ways such as historic analysis or Monte Carlo simulation. The meaning of the number could be explained in a standardized explanatory text. The fund provider should, however, have the opportunity to briefly comment on the number if he wishes to do so, to outline any particularities resulting from specific investment techniques applied.

In regards to currency risk, information should be provided as to what extent the currency risks of the underlying holdings are hedged.

Q29. Is the suggested assessment grid Annex 5 for methodological and presentation issues appropriate and sufficient for identifying a relevant methodology?

None of the existing risk indicators are able to capture all relevant risk factors. If the consumer is to be presented with a single risk number, CESR should make explicit which type of risk is to be estimated. Please see our comments at the beginning of this chapter in regards to risk / return and risk indicators.

Q30. How could the potential limitations of the quantitative calculation of a synthetic risk/reward indicator be further mitigated?

Referring to our comments in the introduction, we do not believe that the concept of a risk / reward indicator should be pursued.

Q31. Do you agree that the possible limitations to a risk reward might be effectively communicated to consumers through textual warnings? Is the proposed wording appropriate?

Referring to our comments in the introduction, we do not believe that the concept of a risk / reward indicator should be pursued.

Q32. Which funds or which risks might not be adequately captured by a quantitative methodology?

Funds or risks may not be adequately captured by a quantitative methodology when the fund exhibits liquidity risks. Such liquidity risks could arise from illiquid or less liquid fund holdings, such as small cap stocks.

Q33. Could the display of scenarios or tables illustrating the behavior of formula funds enhance the information disclosed for those funds? Do you think that such presentations should be limited to formula funds? Do you think that such presentations might have some misleading effects, might be manipulated, or mistaken for a guarantee? How could these be addressed and reduced? Do you think that such disclosure should be made in a harmonized way? What could be possible ways of showing prospective scenarios?

Referring to our comments in the introduction, we do not believe that the concept of a risk / reward indicator should be pursued. The display of prospective scenarios showing the return of the fund are likely to be misleading.

CHAPTER 7 – PAST PERFORMANCE

Q35. Is CESR correct to recommend that information about past performance be included in the KII?

State Street agrees with CESR's recommendation that past performance data should be included in the KII even if a correct interpretation of this information can be difficult. We can confirm CESR's observation that investors consider past performance to be key information. Banning such information from the KII is unlikely to change this perception, especially as such data is readily available elsewhere.

Q36. Has CESR identified the right areas and ways in which this information should be standardized?

We support CESR's view that in regards to both presentational elements and calculation methodologies there should be further standardization similar to what prevails in MiFID. The proposed presentational approach to be tested with consumers with (i) a bar chart layout; (ii) using percentages; (iii) showing average yearly (net) performance and (iv) narrative text to contextualize the information and warn about its limited value as a guide to future performance, strikes us as sensible.

Q37. Which charges should performance figures take into account? For instance, should figures include allowance for subscription and redemption fees?

We would object to the idea of taking subscription and redemption fees into account for a number of reasons:

Firstly to ensure comparability of funds there would have to be agreement on the time period over which fees are to be amortized. For example, where the performance fee is reduced by an entry fee, should this be amortized over e.g. two or three years?

Information in regards to the chosen time period would need to be disclosed as it is likely to influence the holding period of the funds.

Secondly, subscription and redemption fees are typically negotiable. They might be waived completely or reduced depending on the share class / client relationship. A performance fee calculated on maximum applicable subscription and redemption fees might not be representative.

Thirdly, maximum subscription and redemption fees are often adjusted based on broker relationships and distribution channels chosen. This would be difficult to be adequately reflected in a yearly net performance figure without providing further explanation.

CHAPTER 8 – CHARGES

Before addressing the specific questions posed in this Chapter, we would like to share a general observation on this topic. According to CESR, information about charges is “crucial” for retail investors making investment decisions and provides a basis to compare different products. We have made the observation that it is really the net yearly performance which retail investors consider to be key in their decision making process. In regards to comparing products, we would argue that this is best done on the basis of the net yearly performance figure instead of charges, especially as evidence suggests that even relatively simple information about charges bear the risk of being misjudged and misunderstood. We therefore advocate that the charging structure should be presented in the simplest and clearest way possible.

Q38. Has CESR identified the best overall options for including information about charges in the KII?

CESR discusses two options for presenting information on charges and recommends that the Commission should test both with consumers:

Option A – “Improved version of the current approach” focuses on strengthening the existing disclosure by:

- (i) separately outlining charges paid by the investor, “ongoing charges” paid out of the fund’s assets, and other “additional charges” which might apply such as performance fees;
- (ii) removing information which is immaterial for the average retail investor or covered by other disclosed charges (e.g. different components of “ongoing charges”); and
- (iii) making clearer what disclosed charges are and are not covered via a narrative text.

Option B – “Including a summary measure of charges” in addition to the information suggested under Option A.

We believe that CESR has identified the best options for including information about charges. They present the information in a clear way and the chosen labeling should allow the average retail investor to better understand the charging structure.

Of the two options presented, we clearly support Option A. In our view, the addition of a summary measure is likely to mislead consumers. The calculation of the overall charge figure is strongly driven by underlying assumptions such as the holding period. Where these do not reflect the particular situation of the investor it is probably difficult for the average retail investor to understand that the overall charge figures are not representative, but merely illustrative.

Q39. Should a ‘consolidated’ charges disclosure be included, and how should it be described?

Referring to our comments in Q38, we do not believe that a consolidated charge disclosure should be included.

Q40. Should options for the disclosure of charges in cash terms be explored further?

We do not believe that the disclosure of charges in cash terms should be explored further and share CESR's view that presentations using percentages are the better option.

Q41. Do you have any comments on how charges should be organized (e.g. between charges relating to subscribing and redeeming units, ongoing fund charges, and contingent charges), labeled (e.g. 'initial charges,' 'exit charges,' 'ongoing charges') and the accompanying narrative messages regarding what they include or exclude? How much detail is necessary in a document like the KII?

In our view, the example approach to Option A as illustrated in the Paper is a good way to present the information. The charges are both organized and labeled in a clear and easy to understand manner. The content of the accompanying text, however, is best discussed after agreeing whether ex-ante, ex-post or both sets of figures are to be included.

Q42. In relation to the handling of ex-post and ex-ante figures, is it appropriate to include only a single figure for ongoing fund charges in the KII, and if so, on what basis? Do stakeholders have any particular views as to the handling of such information?

CESR outlines four possible options for disclosing ongoing fund charges:

- (i) only ex-post figures, with a statement that the figure may change year to year;
- (ii) only an ex-ante figure, but with an estimate of future expenses;
- (iii) only ex-post figures for ongoing fund charges, but adjusted for any known material discontinuity in the charging structure going forwards; or
- (iv) both ex-ante and ex-post figures.

We do not at this point have a particular view as to the best way to handle ongoing fund charges. In our opinion, a harmonized approach in regards to the calculation of charges needs to be developed. The outcome of the work should drive the question of whether to show the charges on an ex-ante or ex-post basis. As a general comment, however, we would argue that using an ex-ante figure in the KII (Option ii and iv) is probably too difficult. The manager would need to be given the opportunity to disclose to what degree the return could turn out to be a different number, which might confuse the consumer and make the number meaningless.

Q43. How should situations where there is a material change in charging levels be addressed?

While the information itself could be placed in a footnote, the key question is how information regarding material changes in charging levels could be presented in a simple manner. It might be addressed by indicating that the TER, as an ex-post figure reflects the performance net of the old fee, whereas the ex-ante figure is calculated based on the new figure.

Q44. Should portfolio transaction charges be included or excluded from the disclosure of ongoing fund charges? If they should be included, how should assets for which transaction charges are not readily available be handled?

Referring to our comments in Q42, we believe that a harmonized approach in regards to the calculation of charges should be developed first. The outcome of the work should drive the question of whether portfolio transaction charges should or should not be included.

Q45. Has CESR identified the best option for handling performance fees in the KII?

State Street has limited experience with performance fee structures and as such is not well positioned to provide an answer to this question. We therefore choose not to comment.

Q46. Do you agree that CESR should recommend that charges are disclosed on a maximum basis?

We agree with CESR's proposal that all charges in the KII should be based upon maximum levels, with a clear indication that lower figures may apply.

Q47. Are there any options for providing more accurate information, in a way which consumers might understand, about charges under different distribution arrangements?

Referring to our comments in the introduction to this chapter, we do not believe that more accurate information in regards to charges under different distribution arrangements is helpful for the retail investor. Furthermore, Q47 relates to the question addressed in Chapter 4, namely if distribution costs should be systematically unbundled. Referring to our response to Q13, this issue needs to be addressed in a wider context as it is not merely a question of KII, but which distribution model is used.

Q48. Do you agree that CESR should recommend that charges for a feeder fund and its master be combined into a single disclosure in the KII?

We agree with CESR's suggestion that in the case of Option B, the summary measure of charges should combine the charges of the feeder fund and its master.

CHAPTER 9

Q49. Do respondents have any comments on the proposals for consumer testing?

Please see our comments in Q1.

Q50. Do respondents have any initial views on the one-off costs of replacing the SP with KII?

We do not at this point have any views on the one-off costs of replacing the SP with KII.

Q51. Do respondents have any initial views on the on-going costs of KII, compared with those currently included in producing the SP?

We do not at this point have any views on the ongoing costs of the KII.

Q52. What, if any, transitional arrangements should there be if the SP is replaced with KII?

We choose not to comment.

Q53. Is the gradual introduction of KII feasible?

We do not believe a gradual introduction to be feasible.