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Questionnaire on simplified prospectus for retail investors

Background

- The Simplified Prospectus (SP) is a disclosure document designed for retail clients buying units in a UCITS, to provide them with the information they need to make informed decisions about whether to invest in a particular fund or product. The full Prospectus is considered too long and technical for the average investor.
- It is accepted that the current SP is ineffective and needs improvement for the average investor to be able to understand and use it. There have also been problems with the consistency of the information contained within SPs, making it harder for consumers to compare between funds, particularly where cross-border sales are involved.
- In its UCITS White Paper, the Commission proposed developing a new document which is practical and user-friendly. CESR is now keen to seek the views of consumer representatives to better understand what key investor information (KII) can better meet consumer needs.
- The questions and examples below are intended only as a prompt to think about the aspects we need to consider. We are keen to hear any of your concerns or issues about the SP, even if not covered here.

The information to be included

1. *What information should be included?*

   The SP is a mix between key elements and information disclosed mainly for legal reasons. Evidence suggests consumers prefer short documents which do not overload them with detailed and hard to understand information, but that they do not wish to have significant information presented obscurely or hidden away in a separate document or in fine print.

   - Should the information focus only on substantive features of UCITS, with references back to other documents (such as the full Prospectus) or websites for legal information and underlying detail? Would it be acceptable to have key information highlighted in a first part of the document, and then to list less important legal information in a second part? Should certain technical information be explained, with standard examples, in an appendix?

2. *What substantive UCITS features do consumers need to know about?*

   - For example, general information might include details of the fund, its strategy or objectives, any guarantees being included, the type of investor the fund is aimed at, the UCITS' tax regime, the existence or absence of compensation schemes.
   - Should KII target the 'average consumer' (and so fail to meet the needs of less financially capable investors)?

3. *What information should be provided about risks and rewards?*

The SP provides for a detailed list of all possible risks, even if they are very unlikely to happen and of a very technical nature. This presentation does not enable the investor to understand the link between the risks taken and the possible gains. Evidence shows information on potential gains is very appealing to investors, but may also be misunderstood.

- Information about risks can be difficult to present in a simple and easily understood manner. Possible approaches include:

  - ✓ tables or narrative text showing the pros and cons of an investment;
  - ✓ highlighting in general terms only particular risks (e.g. the use of financial leverage) without providing any quantification of their contingency and/or potential impact;
  - ✓ highlighting particular risks with a specification of their contingency and/or potential impact;
  - ✓ a detailed list of all possible risks with or without a description of their contingency and/or potential impact;
  - ✓ a synthetic risk statement, drawn from a scale spanning from "very low" to "very high" risk;
  - ✓ a synthetic risk indicator, drawn from a numerical scale;
  - ✓ a detailed list of all possible risks accompanied by a synthetic risk statement or numerical indicator;
  - ✓ including a statement of minimum recommended investment holding period;
  - ✓ including a minimum recommended investment holding period relating to the synthetic risk statement/numerical indicator of the product.

- Should investors be informed about potential gains as well as risks? Possible approaches include the description of:

  - ✓ the relationship between risk and reward, in a balanced narrative format;
  - ✓ funds past performances only;
  - ✓ funds and benchmarks past performances;
  - ✓ funds and benchmarks past performances and, in case of start-up of innovative funds that have no suitable benchmark, scenarios that illustrate the returns the funds would have earned if launched in the past (back-testing);
  - ✓ funds and benchmarks past performances and, in case of start-up of innovative funds without suitable benchmark, scenarios (tables or graphical tools) that illustrate the returns that could be earned under different (reasonable) hypotheses concerning the future behaviour of the markets targeted by the funds (forward-looking simulation);
  - ✓ funds and benchmarks past performances and, in case of new innovative funds, the results of both back-testing and simulated scenarios;
  - ✓ particular advantages due to the high/low correlation with other products/markets that could be exploited from investing in the fund within a diversified portfolio context.

4. *What information should be provided about strategy and objectives?*

   The SP provides for a detailed description of the strategy pursued and of the objectives of the fund, including the types of financial instruments used.

   - Possible approaches might include providing a brief, plain-language description of main investment features, and, if relevant, the inclusion of any benchmarks (such as official indices or interest rates).

5. *How should past performance information be presented, and for what time period?*

   Evidence suggests that past performance information can be misleading for some consumers. Depending on member states, the SP may include tables, bar charts covering longer periods (10 years) or graphs showing cumulative performance over shorter periods.

- Should information about past performance be presented in a standardised way?
- If so, how? As mentioned above, tables or bar charts or cumulative graphs could be used. *Cumulative graphs tend to obscure the impact of volatility, compared to bar charts expressing in percentage year-to-year variations.*
- Should the display of past performance also be adapted to indicate a recommended holding period?
- Should the KII warn investors about past performance information, for instance by containing a sentence referring to the fact that past performance is no guarantee of future performance?

6. *How should information about charges and fees be presented?*

   Evidence suggests consumers often find it difficult to untangle complicated information about charges. The SP currently includes separate information about ongoing fund charges, by means of a 'total expenses ratio', transaction charges through the 'portfolio turn rate,' and initial or exit charges. All are expressed in percentage rates.

- Examples of approaches include:
    - combining charges into a single figure (alongside or in place of disaggregated charges disclosures);
    - presenting information on charges and other costs in ways that may be easier to understand than percentage rates (if it is thought percentage rates may be difficult for retail investors to understand) ;
    - the use of figures in cash terms, (e.g. showing the effect charges might have on an example investment over different time periods given a standard rate of growth); and
    - explicit disclosure of the commission split between the fund's producer and distributor.
- Should the KII include disclosure of all costs (including transaction costs), even though the information might be complicated and difficult for many investors to understand? If not, which information should be included?
- Is the term 'total expenses ratio' (TER) misleading because it excludes initial, transaction and exit charges?
- Should overall charges be represented in different but complementary ways in the KII: for instance, through a TER which includes initial, transaction and exit charges; and also through a TER without these?

7. *How could the packaging of funds into different end-products be handled?*

   Sometimes UCITS funds are sold as parts of other products, for instance within life insurance or other tax 'wrappers'. These may have their own charges and features and restrictions which the investor will also need to know about. Sometimes these funds and the wrappers are tightly integrated, so it could make sense for information about them both to be combined wherever possible.

- To what extent is it possible for such information to be covered in the KII, given that the fund provider may not be responsible for 'packaging' the fund? What information does an investor need to be aware of from the fund provider?
- How could the KII be varied in content or presentation depending on the context in which the UCITS are being sold?

8. *How far should the information be harmonized between firms and between EU members?*

- How important is it for consumers to be able to compare the UCITS of different firms and those sold cross-border from other Member States?

- What sort of information is most relevant for comparison purposes and should this always be presented in the same way?
- How important is standardisation of KII in promoting investor understanding?
- How should host Member State information (eg where prices are published) be added?

Providing the information to consumers: form and mode of delivery

9. *Would it be useful to specify how this information should be presented?*

   Evidence suggests that consumers respond better to information which is well laid out and visually appealing.

   - Possible approaches include the use of colours, removing small print, highlighting key elements, and the use of standard and clear warnings.

10. *In what form should the information be delivered?*

    - Possible approaches include delivery through the web or by hardcopy. This may depend on the subscription channel used and other conditions of the purchase (for instance, whether it follows advice given by an intermediary, or is the result of a self-made decision).

Timing

11. *How should we ensure consumers get information in sufficient time for it to be useful for their investment decision?*

    Evidence suggests that when the SP is delivered following advice given by an intermediary, this might only happen immediately prior to subscription, with the SP viewed by the intermediary and client as a legal document (contract) rather than a tool aimed at enabling the investor to make an informed decision.

    - Should the approach to providing the KII vary, depending on whether consumers are taking advice, buying directly or not taking any advice on the purchase?
    - Should investors who intend to invest in a UCITS be given a short period in which to consider the key information, before their investment is executed?