



International Swaps and Derivatives Association, Inc.  
One Bishops Square  
London E1 6AD  
United Kingdom  
Telephone: 44 (0) 20 3088 3550  
Facsimile: 44 (0) 20 3088 3555  
email: [isdaeurope@isda.org](mailto:isdaeurope@isda.org)  
website: [www.isda.org](http://www.isda.org)



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**Joint Associations Committee on Retail Structured Products (the JAC) Response to CESR Consultation Papers: “A guide to clear language and layout for the Key Investor Information document (KII)” (CESR/10-532) and “CESR’s template for the Key Investor Information document” (CESR/10-794)**

The Joint Associations Committee<sup>1</sup> welcomes the opportunity to comment on CESR’s proposals as set out in the above Consultation Papers. The JAC has worked to promote a co-ordinated industry approach to improving consumer outcomes for some time, initially formalised by the publishing of the JAC Principles<sup>2</sup> and more recently in our active involvement in responding to both CESR and European Commission consultation processes in relation to UCITS KII and the European Commission’s Packaged Retail Investment Products initiative (the **PRIPs Initiative**). We fully support these initiatives and agree that a correctly structured Key Investor Information regime should be of benefit to both product producers and investors.

We agree that the guidance as set out in the above Consultation Papers will be helpful for market participants. We set out below our suggestions in relation to additional useful guidance which could be incorporated, with a particular focus on structured UCITS funds. Structured UCITS typically have far more detailed disclosure documentation than that used for non-structured UCITS and for this reason the preparation of a KII document in respect of a structured UCITS is likely to be far more challenging than for a non-structured UCITS. This is, therefore, an area in which further CESR guidance will be particularly useful.

To the extent that the proposed UCITS regime will also be influential in determining the shape of the short-form disclosure regime to be developed under the PRIPs Initiative, we also highlight concerns as to the appropriateness of the template and the guidance in the context of the wider range of PRIPs products. In this regard, we refer to our recent supplementary submission to the European Commission in respect of the PRIPs Initiative (the **JAC PRIPs Submission**) which sets out our proposals and concerns in more detail. In particular, we would like to draw CESR’s attention to the pro forma template KII (the **JAC Template KID**) which is the focus of that submission. This pro forma was prepared by members of the Joint Associations Committee for discussion with the European Commission and draws on (i) the work of the Commission, the Council and the Parliament in respect of the review of Directive 2003/71/EC, (ii) the work of the regulators in Hong Kong and Singapore, and (iii) useful concepts raised in the Barclays Capital submission to the Commission in relation to KID of 18 December 2009. We hope that elements of this template would also have useful application in the UCITS sphere and highlight examples of this below. For your ease of reference, we are simultaneously sending the JAC PRIPs Submission, including the pro forma template.

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<sup>1</sup> The JAC’s work is sponsored by interested trade associations; in this instance, the International Capital Market Association (ICMA <http://icma-group.org/About-ICMA.aspx>) and the International Swaps and Derivatives Association (ISDA <http://www.isda.org/>). In the first instance, any queries may be addressed to [rmetcalfe@isda.org](mailto:rmetcalfe@isda.org).

<sup>2</sup> "Retail Structured Products: Principles for Managing the Provider-Distributor relationship" (July 2007) and "Structured Products: Principles for Managing the Distributor-Individual Investor Relationship" (July 2008) which are non-binding best practice guidance produced by the JAC and its members. The full text of the Principles are available at [www.isda.org/press/RSP-Principles071007.pdf](http://www.isda.org/press/RSP-Principles071007.pdf) and [www.isda.org/press/pdf/GlobalPrinciples-sp.pdf](http://www.isda.org/press/pdf/GlobalPrinciples-sp.pdf) respectively.

## CONSULTATION RESPONSES

### **EXECUTIVE SUMMARY**

- Structured UCITS are typically more complex than non-structured UCITS and as a result are currently the subject of far more detailed disclosure documentation.
- This means that the task of preparing a KII document for structured UCITS will be more challenging than for a non-structured UCITS. Given that the page limit is inflexible, material information, including elements of the disclosure suggested in CESR's draft guidance (for example, in relation to risk, telling an investor why a risk is taken, an assessment of the materiality of the risk to the investor and explanations of ways by which a risk is mitigated) will have to be omitted.
- For this reason, more detailed guidance and a separate template for structured UCITS would be of great assistance to the industry. In particular, detailed CESR guidance setting out "safe harbours" for KII preparers when determining what material information can safely be omitted and what information should be considered "self evident" will be important to allow KII preparers to manage disclosure risk.
- The issues presented by lack of space in the UCITS context will only be exacerbated in relation to PRIPs. PRIPs will cover a wide range of structurally diverse products, many of which (Contractual PRIPs<sup>3</sup> in particular) have a more complex risk and reward profile than a structured UCITS.
- The industry would welcome the opportunity to work with CESR both in shaping a "safe harbour" regime and preparing a template KII document for structured UCITS.
- In light of the determinations by other regulators that arbitrary page limits run contrary to policy objectives for KII, we would urge CESR and the Commission to consider carefully whether the imposition of an arbitrary page limit for the PRIPs short form disclosure regime is either necessary or desirable. We highlight below areas where we feel that this would be counterproductive.

### **CONSULTATION PAPER (CESR/10-532): "A guide to clear language and layout for the Key Investor Information document (KII)"**

#### **Part 2 – Using plain language**

##### ***Question 1 – Do you agree with the concepts in Part 2 and that they should form the basis for writing a KII?***

We broadly agree that the principles set out in Part 2 are helpful. In particular:

- we agree with the suggestion that the audience should be assumed to be a "co-operative" and "motivated" individual. If the KII regime is to work, investors must be required to take a degree of responsibility for engaging with the document. We are concerned that responsible investors are not denied useful information

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<sup>3</sup> Please see the distinction made between Contractual PRIPs and Collective Investment PRIPs in the JAC submission to the European Commission in relation to PRIPs of 17 November 2009. The different legal form of Contractual PRIPs has the potential to alter the risk profile, and hence the risk disclosure required, considerably (e.g. the need to disclose issuer credit risk).

due to an undue emphasis being placed on catering for less diligent investors. This would be another element of “dumbing down” which CESR quite rightly suggests should be avoided.

- looking forward, we would argue that more flexibility in relation to length should be built into the PRIPs KII regime whereby clear, succinct and well structured disclosure relating to key information is not removed simply for the sake of meeting arbitrary page limits. Removing such information creates unnecessary disclosure risk for the KII preparer and is detrimental to a diligent investor’s understanding. This would be of particular concern in the context of the wider range of more complex PRIPs products. We note further that other regulators (e.g. the Hong Kong SFC) have acknowledged that arbitrary page limits are counterproductive to the policy objectives for KII. For this reason they have built more flexibility into their KII regimes.
- we agree that in some instances clear language techniques have potential for reducing word count. However, this is not always the case. In particular, the industry often uses jargon as a shorthand for complex concepts or techniques which are nonetheless broadly understood by market participants (for example, “long/short” or “leverage”). Clear, retail investor friendly explanations of such concepts, whilst not needing to be lengthy, may require more space than is available in the KII document. For this reason we support the option to explain such terms in a glossary document. The use of brackets or footnotes may be of use for more simple concepts but risks making the KII document cluttered and disjointed.
- whilst KII regimes have an important role to play in addressing information asymmetry/investor understanding issues, they should not be seen as a panacea. Investor education initiatives and a reformed conduct of business regime are at least of equal importance. In particular, we note that consumer research has concluded that investors place a greater emphasis on their direct interaction with the distributor than they place on any disclosure documentation when making an investment decision.

***Question 2 – Do you have any alternative or additional suggestions?***

None

**Part 3 – Designing a KII**

***Question 3 – Do you agree with the concepts in Part 3 and that they should form the basis for designing a KII?***

We agree with the concepts set out in Part 3. We note, however, that:

- the introductory paragraph refers to subjective concepts such as “grabbing attention”, being “distinguishable” and “appearing important”. These benchmarks will only be useful if specific practical advice as to how they should be met is also offered. Is the intention that the text constituting the rest of Part 3 serves this purpose? If so, could this be specifically noted?
- the limitation of 50-75 characters per line may be restrictive. Given the amount of information to be disclosed (particularly in relation to structured UCITS) this is likely to result in documents with significant amounts of “newspaper” column text, which will be equally unappealing to the eye. Should the aim instead be to have text arranged in a variety of formats (some in wider paragraphs and others in columns)?

***Question 4 – Do you have any alternative or additional suggestions?***

- A technique endorsed by the UK Financial Services Authority for use in key features documents is presenting information in the form of responses to questions which an investor may ask. JAC members agree that this can be an effective method of communicating information to retail investors. This technique was adopted in the preparation of the JAC Template KID. Please see this template for examples of questions which may be relevant.
- Another method which research has demonstrated can assist investor understanding is the presentation of information in the form of graphs, tables and charts. We note that this is already mandated for certain aspects of KII but that in the context of structured products it would also be useful to have the option to present certain data relating to the underlying in these alternative formats. Unfortunately, the page limits under the UCITS regime are likely to preclude this given the additional space required to incorporate these alternative formats. CESR may, however, wish to consider incorporating provisions into the PRIPs regime similar to those found in the Hong Kong SFC's "Key Facts Statement" regime which allows for flexibility in the page limits to allow information to be presented in more investor friendly but space intensive formats.

#### **Part 4 – Guidance for each section of the KII**

***Questions 5 and 6 – Do you agree with the concepts in Part 4 and that they should form the basis for assessing the content of each section of a KII - Do you have any alternative or additional suggestions?***

- We disagree with the statement in **Part 4(b)** that “*you may need to go beyond the prospectus wording to ensure you give a balanced description of the objectives and investment policy*”. Under Article 64 of the revised UCITS Directive, the prospectus is required to include “the information necessary for investors to be able to make an informed judgement of the investment proposed to them, and, in particular, of the risks attached thereto”. It is unclear why CESR would expect a KII document to go beyond the terms of what is required under the Directive. If there is to be such a requirement, clear and specific guidance should be given as to what additional information would be expected.

We note further that requiring further information of this nature also increases risk for the KII preparer as such information could lead to the KII being found to be inconsistent with the prospectus and thus in breach of the applicable liability regime under Article 74.

- We agree that the removal of “self-evident” text (as suggested in **Part 4(b)**) is a useful technique but would suggest that it may not always be easy to determine what might or might not be “self-evident” to an unsophisticated investor. Is it “self-evident” that the regulatory regime applying to a Fund may preclude it from performing certain acts that it states that it will perform in a KII document? As such, is the caveat “to the extent permitted by regulations” not important where a regulation not known to an investor may affect the Fund’s ability/duty to perform an obligation? Flexibility (preferably in the form of “safe harbours”) will be required in the enforcement regime to take account of genuine assessments by KII preparers that information was “self evident” where the benefit of hindsight demonstrates this to have been incorrect.
- Both **Parts 4(b) and 4(c)** discuss the omission of non-material information. We would note in this regard:
  - A determination as to what is and is not material will be one of the most challenging aspects of completing a KII. It is far easier to judge materiality with the benefit of hindsight and, as such, significant allowances will need to be made in the enforcement regime where genuine assessments on behalf of KII preparers later prove to be incorrect. Again, we would suggest that clearly defined “safe harbours” would be the best way to address this issue. With this in mind, more detailed process-based guidance from CESR as to how to determine what information is and is not material in the context of

KII, and which risk disclosure can safely be left to the prospectus (as cross referenced in the KII) would be useful.

- The information suggested in Part 4(c) in relation to materiality of risks, (i.e. that the KII sets out “how likely it is that a particular risk will materialise, and how severe the impact would be if it did”) would seem particularly problematic. Risks by their very nature are difficult to predict with certainty and providing such an assessment would leave the KII preparer a hostage to fortune.
- In relation to structured UCITS in particular, the strict page limit prescribed means that in many cases excluding only immaterial information will not be sufficient and that, to meet the page limit, material information will also have to be omitted. Whilst this is perhaps undesirable (and in this regard we note our comments above in relation to the counterproductive effectiveness of rigid page limits), the mandated page limit makes this inevitable. This is clearly a source of significant potential risk for KII preparers. As such, for structured UCITS, the guidance as to a “safe” approach to selecting which material information can be omitted from a KII as suggested above would be particularly valuable.
- The section titled “Special Considerations for structured UCITS” in **Part 4(b)** might benefit from being broken down into appropriately categorised sections (e.g. split into those considerations relating “Scenario Analyses”, those relating to “Formula” and those relating to “Guarantee/Capital Protection”). Furthermore, might the considerations in relation to altered risk and reward profile and the risk of capital loss at specified trigger dates be better placed in a separate “Special Considerations” section in the Risk and Reward section (i.e. Part 4(c)) of the guidance.
- **Part 4(c)** appears to contemplate the inclusion of significant quantities of narrative explanation in addition to the Synthetic Risk Reward Indicator (**SRRI**) and mandated accompanying text. This includes, for example, telling an investor why a risk is taken, an assessment of the materiality of the risk to the investor and explanations of ways by which a risk is mitigated. As noted above, whilst this would clearly all be useful information for an investor, for the majority of products, there will not be sufficient space for it to be included. This should be recognised in the guidance by splitting this section into two parts: (i) the core information required for all products, and (ii) this further information (as set out above) that would be of assistance where space permits.

We note further that the need to include significant explanatory text to accompany the SRRI is one of the reasons why the JAC PRIPs Submission argues that the SRRI should not be included in the PRIPs short-form disclosure regime. In the context of more complex products (including structured UCITS) it is unhelpfully reductionist and detracts from, and reduces the space available for, more valuable narrative explanation.

- We would question whether the statement in **Part 4(c)** that risk only relates to “uncertainties” reflects the way in which an investor would analyse a product. Please see the JAC PRIPs Submission and the JAC Template KID and the way information is split between the Product Description and Key Risks section therein. After lengthy consideration as to how best to apportion information it was determined that the Product Description should address the intended return of the product (i.e. if held to term (if applicable) and with no unforeseen disruptions having occurred) and any provisions which would result in the potential disruption or reduction of this return (or restrict an investor’s ability to realise their investment at its full value at any given time) should be disclosed as a risk, that being the way in which we felt an investor was likely to view such provisions. Where necessary the completion notes to the JAC Template KID suggest that cross-references be included in the Product Description referring investors to the appropriate explanation in the Key Risks section. This assists the investor in navigating the KII and ensures that

disclosure of risk and potential reward is, at all times, balanced. CESR may wish to consider whether a similar approach to determining what is or is not a risk is adopted for the purposes of the UCITS KII.

- We agree that the grouping of risks is a useful technique to assist comprehension. Please see the JAC Template KID for possible risks categories which we have identified.
- We agree that the ability (as set out in **Part 4(d)**) to cross-refer to more detailed charges information in the prospectus is valuable. This reduces the need for unnecessary detail in the KII whilst at the same time assisting investors to effectively utilise the full range of disclosure information available to them. CESR may wish to consider whether it would be helpful to provide more detailed guidance as to which charges information it is acceptable to leave to be disclosed in the prospectus and which information must appear in the KII.
- In relation to **Part 4(f)**, it might be useful for investors if sub-headings were included in the Practical Information to categorise the information provided (for example, “Further information available to you”, “Taxation”, “[X]’s Liability” etc). In the JAC Template KID this section has been divided out into a number of different sections to make the information more readily identifiable, and, therefore, accessible, to investors. Please note further, that in context of PRIPs short form disclosure regime, we would suggest that the disclosure relating to “Taxation” is moved to the “Charges” section (as per the JAC Template KID). We feel that it would be easier for investors if all amounts potentially deductible from their investment are disclosed in the same section.

**CONSULTATION PAPER (CESR/10-794): “CESR’s template for the Key Investor Information document”**

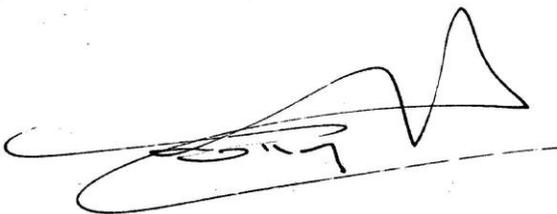
***Question 1 – Do you find the attached template useful?***

We agree that a template setting out the content and layout for the KII is useful.

***Question 2 – Do you have any other suggestions?***

- The template states that it applies to “standard” UCITS only. We assume that this means that this would not include structured UCITS. It would be helpful if CESR produced a template in respect of structured UCITS reflecting the alternative information requirements for those products and presentational advice in respect of the scenario analyses. The industry would welcome the opportunity to work with CESR in producing such a template.
- The first three bullet points in the Risk and Reward Profile section<sup>4</sup> are likely to be common to all KII documents. CESR may wish to consider suggesting non-mandatory wording for such warnings to assist KII preparers.
- We note that even before the completion of the narrative disclosure in the Objectives and Investment Policy and Risk and Reward Profile sections and the details of where and how to obtain further information in the Practical Information section, the template already runs to two pages. Please see the concerns expressed in our responses to Consultation Paper (CESR/10-532) regarding page limits, particularly in the context of more complex structured UCITS. These issues are likely to be further exacerbated in the context of the more diverse and complex range of PRIPs products.
- Charges figures are to be expressed as a percentage figure. What should this be a percentage of?

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Timothy R Hailes', written over a horizontal dashed line.

Timothy R Hailes  
Chairman – Joint Associations Committee on Retail Structured Products

JAC contact - Richard Metcalfe, ISDA  
[rmetcalfe@isda.org](mailto:rmetcalfe@isda.org), 0044 20 3088 3552

<sup>4</sup> i.e. statements to the effect that (i) historical data may not be a reliable indication for the future, (ii) the risk category shown is not guaranteed and may shift over time and (iii) the lowest category does not mean “risk free”.