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CEIOPS' Reply to CESR's Consultation Paper on content and form of Key Investor Information disclosures for UCITS (CESR/07-669)

In order to answer to the European Commission's request for assistance on the form and contents of Key Investor Information ("KII") as a possible replacement for the Simplified Prospectus for UCITS, CESR has issued in October 2007 a Consultation Paper ("CP") with a deadline for answers by 17 December 2007.

This request should be seen in the context of the Commission's wider work to encourage informed decision-making by potential retail investors and, more in particular, to revise the UCITS' Directive.

CEIOPS appreciates CESR's effort and hard work on KII. CEIOPS supports the main objective of the CP that according to the European Commission's concern is "to replace the existing simplified prospectus with short, meaningful explanations of the risks, costs and expected outcomes associated with investment in a UCITS [...] in short and simple form, understandable to retail investors[1]. The aim is to enhance the disclosure requirements for policyholders, but also to reduce costs for the operator and to foster harmonisation between Member States, in order to assist comparisons between funds, particularly when cross-border sales are involved[2].

CEIOPS notes that CESR limits the scope of the CP by declaring to be "unable to make specific recommendations (in situations where other Directives are applicable, e.g. in relation to insurance products) because the interactions between different Directives raise issues that require broader consideration"[3]. Indeed, CEIOPS has not been consulted "at this stage" of the KII analyzing procedure [4].

CEIOPS would, however, like to share already some views with CESR, since, as CESR acknowledges, "in some jurisdictions, significant volumes of UCITS retail business may be conducted by repackaging the UCITS as a life insurance product"[5]. In addition, CESR further refers to insurance products in relation to "wrappers"[6], in which CESR classifies unit-linked insurance contracts as a kind of "wrapper", along with retirement products, investment management agreements or structured products[7].

Simplified information and a user-friendly form is however equally important for policyholders of unit-linked life insurance products. This is particularly relevant for complex insurance products which characteristics can sometimes be trickier than the ones of the direct holdings in UCITS funds. The use of UCITS disclosures themselves for some unit-linked products, either as a template or passed on to the investor where the UCITS is one of the underlying assets, is likely therefore to raise significant issues requiring careful consideration.

CEIOPS shares the Commission's and CESR's objective to focus on evidence-led policy making in this work, with robust testing with consumers as a key step in fostering

1 CP p. 18 – Reference to the letter of the EC

2 CP p. 10 – Reference to the letter of the EC

3 CP par 3.9 (p. 14)

4 CP, par 3.2. (p. 13)

5 CP par 3.32 (p.16)

6 CP par 3.33 (p. 17)

7 CP par 3.13 (p. 14)

documents consumers will actually use. This objective is even more important for policyholders with regard to some characteristics of unit-linked life insurance products:

- The choice of the UCITS in which to invest as units is only one element of choice. The policyholder also should understand the functioning and characteristics of the insurance contract itself. While simpler and clearer information about the UCITS is valuable, there are likely to be challenges around the ‘fit’ between the fund-level disclosures and those at the level of the product to ensure investors understand the nature of the combined proposition. For instance, the design of the product may have important features which modify the behaviour, risks and cost characteristics of underlying funds. Particular units may not perfectly mirror UCITS, even where they are solely invested in a specific UCITS. Charges may be materially different to those disclosed for underlying UCITS. Different tax treatments at the fund level could significantly modify performance.

- An investor in a UCITS has a direct holding in that UCITS, whereas an investor in the UCITS by means of a life insurance wrapper would not have a direct holding, such that some of the information in a KII might be irrelevant or misleading.

- The time horizon of the insurance contract is often much longer than the minimal or even recommended investment period of the UCITS. The policyholder may then have to reallocate its investment.

- Policyholders are often advised to mitigate the risk by investing the insurance premiums in diversified UCITS with different level of risks, and to assess the overall level of accepted risk. This requires good and accessible information on the risk associated with each UCITS. However, the combined risk/reward behaviour may be difficult for investors to grasp by looking at ratings for individual funds. Since the UCITS work is focused on individual fund disclosures, it is not likely to directly address this issue.

- Some insurance contracts offer to invest in many (up to a few hundreds) UCITS. Some will also offer assets / funds which are not UCITS, raising problems for investors where inconsistent disclosures are made for different funds (e.g. KII for some funds, other standardised disclosures for some other funds/assets, and potentially no standardised disclosures for some funds/assets). While the KII may form a useful element of the wider disclosure picture, it is important again to consider the overall effectiveness of the information provided about insurance contracts and the funds available under them.

Furthermore, CEIOPS would like to make some suggestions to increase the effective use of KII for UCITS serving as units in life insurance products.

- The work on KII might feed into effective disclosures for units in life insurance products. While there may be difficulties in using KII un-amended or without being accompanied by additional information, consistency with the KII (or in certain circumstances its direct use) would be a good starting point for finding an overall disclosure approach for unit-linked contracts which investors actually understand and use. Consumer testing of any approach would be just as important for unit-linked life insurance contracts as for UCITS, particularly given the additional complexity of some of these contracts.

- Concerning the issue of capital guarantees, policyholders sometimes tend to consider that since they invest in an insurance product, all guarantees or commitments mentioned in documents that are part of the insurance contract rely in one way or another on the insurance company. CEIOPS therefore notes that the nature of any guarantees referred to must be crystal clear, and supports an option of reserving the term of guarantee for when a legal guarantee is given, potentially with an indication of the guarantor should this prove useful for investors, so that the policyholder is clearly informed that this is not the insurance company.

- Concerning the disclosure on risks, CEIOPS would like to express its interest in the future result of the work on UCITS used in a “wrapper”. Indeed, most unit-linked insurance contracts are invested in multiple UCITS and an indication of the overall level of risk would certainly be helpful for the policyholder, as mentioned above.

- CESR assumes that the fiscal drive is the only reason for the rise in unit linked "wrapping UCITS". CEIOPS would like to point out that the fiscal drivers noted by CESR are not the only reasons for this rise. For instance in the Italian case, fiscal advantages have been abolished yet unit-linked policies are thriving. Moreover, in the report on substitute products, the authorities from eight Member States put forward additional insurance features as influencing the investor choice towards unit-linked insurance products, among them life cover and cover of mortality risks, the opportunity to depart from common rules on inheritance, or the fact that insurance contracts can’t be seized. Other issues include the flexibility they can offer for gaining access to a range of asset classes (since switching facilities may not trigger tax events which would be triggered outside an insurance wrapper; such facilities can be common for defined contribution occupational pension schemes).

CEIOPS appreciates that further work is needed to foster consumer protection through an adequate and harmonised information approach. CEIOPS will be happy to assist CESR and the European Commission in this project.

For further information, please contact

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