

Asset Management Market Study - further remedies

Policy Statement

PS19/4

February 2019

This relates to

Consultation Paper 18/9
which is available on our website at
www.fca.org.uk/publications

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1 Summary

Introduction

- 1.1** In our Final Report on the Asset Management Market Study (AMMS), we set out evidence of weak price competition in a number of areas in the asset management sector. This matters to millions of people who use the services of the asset management sector directly, or indirectly through their pensions.
- 1.2** In response to the AMMS, we set out a package of remedies designed to improve competition in this sector. They seek to address both demand side and supply side problems in the asset management industry. They should lead to greater competition and innovation in this market to the benefit of consumers.
- 1.3** In April 2018, we published a Policy Statement, [PS18/8](#). This set out our final rules and guidance to improve fund governance for authorised funds and outcomes for investors by moving them to better share classes and ensuring fairer allocation of dealing profits.
- 1.4** This Policy Statement (PS) is our response to Consultation Paper (CP) 18/9: [Consultation on further remedies – Asset Management Market Study](#). It summarises the feedback we received to that consultation and our responses. It also sets out the final rules and guidance.
- 1.5** CP18/9 proposed measures to improve the quality, comparability and robustness of the information available to investors. Those proposals aimed to address our concern that fund objectives are not sufficiently clear or specific, making it harder for investors to make the right choices.
- 1.6** We also proposed measures to improve transparency in cases when funds have limits in how far their holdings can differ from a particular benchmark or index.
- 1.7** We consulted on the following proposals:
- new non-Handbook guidance to remind authorised fund managers (AFMs) how they should describe fund objectives and investment policies to make them more useful to investors
 - requiring AFMs to explain why their funds use particular benchmarks or, if they do not use a benchmark, how investors should assess the performance of a fund
 - requiring AFMs that use benchmarks to reference them consistently across the fund's documents
 - requiring AFMs that present a fund's past performance to do so against each benchmark used as a constraint on portfolio construction or as a performance target
 - amending our rules to require that where a performance fee is specified in the prospectus, it must be calculated on the basis of the scheme's performance after the deduction of all other fees

Who this affects

- 1.8** This PS is relevant to UK AFMs who manage authorised funds (open-ended collective investment schemes).
- 1.9** This paper will be of interest to other firms in the investment management industry, such as those acting as delegated portfolio managers, depositaries of authorised funds and financial advisers. It will also interest industry bodies. Given the number of consumers affected by the asset management industry, consumers and their representatives may also find it relevant.
- 1.10** The remedies are also potentially relevant to unit-linked and with-profits business. We are carrying out diagnoses of with-profits and unit-linked products, which will improve our view of any harms in these markets. We will conclude this work later in 2019. We will then decide whether we need to carry out further intervention into unit-linked and with-profits products and the most appropriate way for us to do this. We expect to publish our view on this in 2019.

The wider context of this policy statement

- 1.11** The asset management industry plays an important role in the UK's economy. Asset managers look after the savings and pensions of millions of people, seeking returns by investing in a variety of assets. They allocate capital to the businesses that they think are most likely to grow, and contribute to corporate governance in the companies that they invest in.
- 1.12** The AMMS presented evidence of weak price competition in many areas of the asset management industry. This matters because it means lower returns for investors.
- 1.13** PS18/8 set out a package of measures to address the supply side weaknesses the AMMS identified. The rules in this PS complement the work to improve the transparency of costs, charges and performance of the products investors buy.

Fund Objectives Working Group

- 1.14** We set up the Fund Objectives Working Group (FOWG) to help inform our proposals in this paper. As part of the working group, it was agreed that the Investment Association (IA) would work with its members and consumer representatives, informed by consumer research, to promote the use of consistent terminology in communications from fund managers about their funds. We understand the IA will publish their guidance on fund communication in February 2019.

Institutional Disclosure Working Group

- 1.15** The AMMS found that institutional investors find it difficult to get the cost information they need to make effective decisions. To remedy this, the FCA set up the independent Institutional Disclosure Working Group (IDWG). The IDWG recommended the use of five templates for data collection and disclosure by asset managers to institutional investors. In November 2018, the Cost Transparency Initiative (CTI) was launched to take the recommendations of the IDWG forward, supported by the Pensions and Lifetime Savings Association (PLSA), the IA and the Local Government Association (LGA).

Referral to the Competition and Markets Authority

- 1.16** In September 2017, the FCA made a market investigation reference (MIR) to the Competition and Markets Authority (CMA) on investment consultancy and fiduciary

management services. These markets include advisory and investment services provided mainly to pension trustees. The AMMS found that some features of these markets may restrict or distort competition. We considered the CMA was best placed to carry out a review because these services are largely outside the scope of our regulation.

- 1.17** In December 2018, the CMA published its findings that there is an adverse effect on competition in the investment consultancy market and the fiduciary management market from which substantial customer harm may result. The CMA's Investment Consultants Market Investigation Final Report introduces a package of remedies to address the negative effects on competition they identified.

How it links to our objectives

- 1.18** Our new rules and guidance are intended to advance our objectives of securing an appropriate degree of protection for consumers and promoting effective competition in the interest of consumers.

Outcomes we are seeking

- 1.19** If the remedies set out in this PS are successful, it will make it easier for investors to choose the best fund for them and help them achieve their investment objectives. Our performance fee proposal will promote fairness in how these fees operate.

Measuring success

- 1.20** We will assess through our supervisory and authorisations work whether our interventions are effective. We expect to see clearer and more meaningful fund objectives and more consistent disclosure where benchmarks are used. In addition, given the continued importance we attach to the success and reform of the sector, we will undertake a check on the impact of the overall reforms as a whole in 12 and 24 months and publish a brief update.

Summary of feedback and our response

- 1.21** We received 39 responses to the consultation from across the asset management industry and consumer groups.
- 1.22** Most respondents supported the proposals set out in CP18/9. We are, therefore, proceeding on the basis on which we consulted, with minor drafting amendments in a few areas to improve clarity and ensure that the policy intention is achieved. In particular, neither the Handbook instrument nor the non-Handbook guidance differ significantly from the drafts consulted upon.
- 1.23** This PS includes a summary of the feedback we received, and our response, in Chapters 2, 3 and 4. The final rules and guidance we are making can be found in Appendix 1 and 2.
- 1.24** We would like to thank all respondents for taking the time to share their views.

Equality and diversity considerations

- 1.25** We have considered the equality and diversity issues that may arise from the final rules and guidance in this PS. Overall, we do not consider that they adversely impact any of the groups with protected characteristics i.e. age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment. No respondents to CP18/9 raised any concerns about equality and diversity considerations.

Next steps

- 1.26** We set out final Handbook text in Appendix 1 and non-Handbook guidance in Appendix 2. The new Handbook rules and guidance covered in the "Benchmarks" section come into force on 7 May 2019 for new funds and on 7 August 2019 for existing funds. Our rules on performance fees come into force on 7 August 2019. In addition, we are clarifying how Chapter 4 of the Conduct of Business sourcebook (COBS 4) applies to the key investor information document and this change will come into force on 4 February 2019.
- 1.27** We expect AFMs to take our guidance on fund objectives into consideration when reviewing fund documentation from the date of publication.

2 Fund objectives

- 2.1** In this chapter, we summarise the feedback we received on our proposals to improve the clarity and usefulness of fund objectives for consumers, and give our responses.

Fund objectives and investment policies

- 2.2** In broad terms, fund objectives and investment policies, which in this chapter we collectively call 'objectives', are statements of what a fund aims to achieve and the way it intends to do so. Objectives and policies include, for example, a description of what a fund can invest in and any limitations on fund investments. Consumers rely on this information to help them compare their investment options and to choose which funds to invest in.
- 2.3** The AMMS found that objectives are not always as clear and helpful to consumers as they could be. We expect fund managers to explain what their funds are doing in consumer-friendly language. Clear and helpful objectives should mean better informed consumers making decisions to invest in funds that are more suited to their individual needs and expectations.
- 2.4** As set out in CP18/9, we consider that the existing rules on objectives and the disclosure of objectives are adequate and we do not propose to change them. Instead, we are publishing non-Handbook guidance to set out our expectations of how firms might comply with the existing requirements on fund objectives in practice. We asked:

Q1: Do you agree with our draft guidance on fund objectives?

Feedback received

General issues

- 2.5** Most respondents broadly supported our draft guidance on fund objectives. Respondents agreed that the level of detail on objectives for consumers in key information documents, such as the UCITS Key Investor Information Document (KIID) and the PRIIPs Key Information Document (KID), is inconsistent between funds and that new guidance will help to remedy this. A couple of respondents argued that we should be making rules - instead of guidance - on the description of fund objectives, as they believed that new guidance will not be enough to change industry practice.
- 2.6** A minority of respondents were concerned that new guidance will require firms to implement new internal governance and sign-off processes to ensure that the way they communicate objectives in prospectuses, key information documents and marketing communications meets our expectations. They argued that the benefit of the new guidance for consumers will be outweighed by the increased administrative burden on firms.

Clarity of objectives

- 2.7** Most respondents supported clearer objectives for consumers, but a significant number of respondents raised concerns about the difficulty of describing objectives clearly and concisely. They explained that investment industry terms are often complex. Many of these respondents also said that the mandatory key information

documents, such as the KIID, do not provide adequate space for consumer-friendly explanations of complex terms. One respondent cited "growth investing" as an example of a common phrase that would be difficult to explain concisely to a consumer. A few of these respondents said it would be helpful if we provided more examples of good and bad practice when describing objectives. A couple of respondents suggested that we should publish a glossary of consumer-friendly terms to help fund managers describe objectives to consumers.

2.8 The draft guidance set out that a fund manager should generally include a description of the investment strategy in key information documents where it is necessary to describe the objectives and investment policy. Some respondents asked whether investment strategies should be included in key information documents. A few argued that all consumers need, when comparing risk profiles between funds, is a list of the assets and instruments that the fund can invest in.

2.9 Some respondents emphasised the importance of objectives that provide the fund manager with the flexibility to respond to changes in market conditions.

Non-financial objectives

2.10 Most respondents agreed that we should clarify our expectation about the description of non-financial objectives. The draft guidance sets out that non-financial objectives must be explained to consumers in a way that is fair, clear and not misleading. Many respondents were concerned about our expectation that firms setting non-financial objectives must also explain clearly to consumers how they will measure whether investments are meeting non-financial objectives. Respondents said that non-financial objectives are difficult to measure and often require qualitative, rather than quantitative, analysis. Some respondents noted that environmental, social and governance (ESG) objectives can be financial as well as non-financial. Others argued that we should issue more substantive guidance in this area.

Our response:

We have considered the feedback and we will be proceeding with the guidance we consulted on. We have made some minor amendments to the description of fund objectives and investment policies to clarify our intentions. The final non-Handbook guidance can be found in Appendix 2.

We believe the new guidance will help fund managers to make objectives more meaningful and useful to consumers. This in turn will help consumers to compare their investment options more effectively and make investment decisions more closely aligned to their needs and expectations.

General issues

The Government has announced its intention that the UK should leave the EU on 29 March 2019. Whilst the UK remains a member of the EU, we are unable to make rules which would require a fund manager to provide additional information in the UCITS KIID or PRIIPs KID because the form and content of both documents are set out in maximum-harmonising legislation.

We do not agree that the new guidance will significantly increase administrative burdens on firms. Our guidance clarifies our expectations for describing objectives under the existing requirements, and explains how firms might comply with these requirements in practice. We consider that a firm should be able to take on board the points we make in our guidance without significantly adding to the costs in this area.

The IA has been carrying out work, including detailed consumer testing, to help its members to explain fund objectives more clearly and in a way that retail consumers can understand. We welcome this work.

Clarity of objectives

We do not currently have any plans to publish examples of good and bad practice, nor do we plan to publish a glossary of consumer-friendly terms. Fund managers will need to consider whether consumers can reasonably understand the objectives they set out.

We have amended the final guidance to clarify our expectations around the disclosure of investment strategies. We expect fund managers to disclose in key information documents the features of the investment strategy that are a fundamental feature of how the product is managed. For example, where the manager's strategy is to invest only in companies that they consider to have good growth prospects, we expect this to be disclosed. Where a manager has flexibility to invest in different ways depending on their view of market conditions, we would not expect them to disclose the investment focus at a single point in time in the KIID or prospectus. In this case, they should make clear the flexible nature of their investment strategy.

CP18/9 recognised there is a tension between having objectives that are specific enough for investors and flexible enough for fund managers to adjust investments in response to, or in anticipation of, changing market conditions. We recognise that it may be in consumers' interests for fund managers to keep the flexibility to change the make-up of a portfolio or the investment strategy in response to market conditions. We do not consider these two aims are incompatible and expect fund managers to manage this tension in a way that is in the interests of consumers.

Non-financial objectives

An increasing number of firms set non-financial objectives for their funds, including ESG objectives. Our new guidance on non-financial objectives reminds fund managers that we expect non-financial objectives to be fair, clear and not misleading. This is no different from our expectations for financial objectives. We agree that ESG objectives can be financial as well as non-financial.

3 Benchmarks

3.1 In this chapter, we summarise the feedback received, and provide our responses, to our proposals to:

- make new rules requiring AFMs to explain why they use particular benchmarks or, if they do not use benchmarks, to explain how investors should assess the performance of the fund
- require that, if a fund manager uses benchmarks, the benchmarks must be referenced consistently across the fund's documents
- require that, whenever the fund manager presents the fund's past performance, it must do so against each benchmark used as a constraint on portfolio construction or as a performance target

3.2 In CP18/9, we set out 3 benchmark categories that were relevant to our proposals.¹ These were:

1. A 'constraint' - an index or similar factor that fund managers use to limit or constrain how they construct a fund's portfolio
2. A 'target' - an index or similar factor that is part of a target a fund manager has set for a fund's performance to match or exceed, which includes anything used for performance fee calculation
3. A 'comparator' - an index or similar factor against which a fund manager invites investors to compare a fund's performance

Use of benchmarks

3.3 We have found that fund managers rarely explain why or how they are using particular benchmarks. Some of the ways fund managers use benchmarks include as a constraint on how they construct a fund's portfolio, as a target for fund's performance, or as a way for investors to compare the fund's performance.

3.4 We consulted on rules requiring fund managers to explain in a fund's prospectus and consistently in other consumer-facing communications that include fund-specific information, why they have used any constraint, target or comparator benchmark. Where a fund does not use a benchmark, we proposed that a fund manager should explain in the fund's prospectus and relevant documents how investors should assess a fund's performance.

3.5 In CP18/9 we asked:

Q2: Do you agree that we should introduce a 'requirement to explain' with regard to AFMs' use of benchmarks?

Q3: Do you agree that we should introduce rules and guidance to require consistency in references to benchmarks across the same fund's documentation?

¹ As set out in CP18/9, these proposals are entirely separate and have no bearing on the EU Benchmarks Regulation.

Feedback received

General

- 3.6** Respondents broadly supported our intention to improve the information given to investors. They also agreed it was necessary for fund managers to explain how they used benchmarks. There were some practical comments on how we could improve aspects of the proposals. There were some concerns that our proposals would lead to increased costs in accessing benchmarks. We discuss this further in Chapter 4.

Definition of benchmarks

- 3.7** Most respondents agreed with the three categories of benchmarks we set out in the consultation. However, some respondents felt that our definition of a benchmark was not clear enough. Some respondents conflated benchmarks that influence the portfolio construction process with those that are used after the portfolio's construction by fund managers and others to assess performance (comparators). Some also said that benchmarks used for remuneration policy or risk management should not be captured by our rules as, they argued, they do not affect a manager's decisions about portfolio construction.

- 3.8** Some of the feedback suggested that our view of a benchmark being an index or 'any other similar factor' will lead to uncertainty.

Funds not managed with reference to a benchmark

- 3.9** Where a fund has no constraint or target and invests in multiple asset classes, some respondents argued that there is often no appropriate comparator. In such cases, feedback was split between those who thought investors should be invited to compare performance against a benchmark of their own choosing, which is appropriate for their purposes, and those that thought that it was the fund manager's responsibility to explain to investors how to assess performance.

- 3.10** Some respondents said our rules will have the unintended consequence of forcing funds to disclose a benchmark, even if it is not relevant to the way a fund is run, as investors may be less comfortable with funds that don't include a benchmark.

Scope

- 3.11** Most of the responses agreed that the use of benchmarks should be disclosed consistently across a fund's documentation. One respondent said that requiring funds to disclose the use of benchmarks in any relevant communication about a fund would be too broad; they said this could potentially lead to disclosure in unintended situations.

Our response

We are proceeding with our proposals on use of benchmarks.

Definition of benchmarks

We consider the three categories of benchmarks capture the different ways we have seen fund managers use benchmarks in practice. We think these categories can be understood by investors, who are the intended target of these disclosures.

When a fund manager doesn't explicitly manage a portfolio in line with a benchmark, there may still be cases where other factors, such as internal

restrictions or the remuneration policy, mean that the fund is effectively managed with reference to a benchmark. We have provided non-Handbook guidance for when other factors affect the way a fund is run. The final non-Handbook guidance is at Appendix 2.

Funds not managed with reference to a benchmark

We agree that some funds will not be managed with reference to a benchmark. There may also not be a readily available benchmark that corresponds with the way a fund is run. However, fund managers must still be able explain how else to assess their fund's performance.

We do not agree that where a fund has no benchmark, it should be up to the investor to assess a fund's performance. As set out in CP18/9, we want investors to get improved information to explain what a fund does, how it does it and how to evaluate how well it is doing.

The use of benchmarks is not mandatory and we do not expect fund managers to refer to a benchmark if it is not relevant to the way a fund is run. Our rules do not require or encourage fund managers to use benchmarks, but will require that fund managers explain why they have chosen a particular benchmark.

Scope

In CP18/9, we clarified that our requirement to explain the use of benchmarks applied to a fund's prospectus and other consumer-facing communications that include fund-specific information. This does not include general 'brand only' adverts or communications (image advertising). We believe this strikes the right balance between ensuring investors have the information they need and firms not having to provide unnecessary information.

We did not intend the new rules to apply to the UCITS KIID or the KIID equivalent for a non-UCITS retail scheme (NURS). We have decided to make clear that the rules in COBS 4 do not impose obligations on firms to add further information to the UCITS KIID (or the NURS equivalent). This is because legislation already sets out the form and content of the UCITS KIID in an exhaustive manner.

Past performance

- 3.12** In some cases, past performance is presented against different benchmarks across a fund's consumer documents. We proposed that whenever the fund manager presents the fund's past performance, it should do so against each benchmark used as a constraint on portfolio construction or as a performance target.
- 3.13** The UCITS KII Regulation requires firms to disclose benchmarks where used and display performance against such benchmarks. Funds' constraints or performance target benchmarks should appear in the Objectives and Investment Policy section of the KIID.

3.14 Where a fund manager uses comparator benchmarks, we are not making it mandatory to show past performance against such benchmarks. However, if a fund manager chooses to show past performance against one or more such benchmarks, they must do so consistently across a fund's documentation.

3.15 In CP18/9 we asked:

Q4: Do you agree that we should introduce rules and guidance on which benchmarks should be displayed against a fund's past performance, where past performance is shown?

Feedback received

Funds with more than one benchmark

3.16 There was general agreement with our proposals on past performance, although some respondents felt that a fund manager should not be required to show past performance against all identified benchmarks. They argued that showing past performance against multiple benchmarks could confuse investors, rather than help them.

3.17 Views were split among those who thought that not all benchmarks should be shown against past performance. Some thought that the fund manager should always refer to the more ambitious benchmark, while others thought a fund manager should have the flexibility to choose the most appropriate benchmark to show past performance against.

3.18 Respondents also asked whether it was possible to show performance against multiple benchmarks in the current format of the KIID.

Our response

Funds with more than one benchmark

In CP18/9 we set out our expectation that when a fund shows its past performance in a relevant communication, it must do so against each target or constraint a fund has. For funds with more than one such benchmark, we will expect past performance to be shown against all those benchmarks.

The purpose of these proposals is to give investors the information they need to make decisions. Part of that involves consistent disclosure of the use of benchmarks across all relevant communications. Allowing selective disclosure of benchmarks when it comes to past performance would not be consistent with this.

We agree that the text in proposed rule COBS 4.5.14R could be incorrectly interpreted as indicating that we expect funds to show past performance against only one benchmark. We have amended the final rule so that it is clear that a fund should show past performance against more than one benchmark if it uses more than one.

4 Other issues raised

- 4.1** In this chapter, we summarise other issues that were raised in the feedback we received and set out our response.

Performance fees

- 4.2** We consulted on rules clarifying that where a performance fee is specified in the prospectus, it must be calculated on the basis of the fund's performance after all other charges have been deducted. Previously, we only had guidance to this effect.

Our response

Respondents agreed with this proposal, and many said it was already best practice in the market to calculate performance fees after all other charges. We have therefore made the rules as per our consultation.

Implementation period

- 4.3** A few respondents argued that implementing the guidance on fund objectives would require significant effort and so there should be an implementation period. Similarly, there were concerns that the 3 and 6-month implementation periods for the benchmark proposals would cut across the implementation date for the PRIIPs Regulation applying to UCITS funds. Some respondents said fund managers may have to update fund documentation twice within a short period of time.

Our response

Our guidance on fund objectives reflects our expectations on how to satisfy existing requirements. Firms may rely on the guidance from the date of publication.

On the benchmark proposals, it now appears likely that the transitional period for use of the UCITS KIID under the PRIIPs Regulation will be extended until the end of 2021. Therefore, we will proceed with the 3 and 6-month implementation periods on which we consulted.

Estimation of costs

- 4.4** Some respondents said our proposals would lead to greater use of benchmarks and therefore increase the cost of accessing benchmarks. As a result, they did not believe that our cost benefit analysis in CP18/9 accurately captured all the costs that fund managers would have to bear.

Our response

Our rules do not place a new requirement on fund managers to use a benchmark. Therefore, our rules should add no direct additional cost where funds do not use a benchmark.

Annex 1

List of non-confidential respondents

Amundi

Association of Investment Companies

BNY Mellon

Brian Shearing and Partners

CFA UK

Close Brothers Asset Management

CMS Cameron McKenna Nabarro Olswang

DATA

Equitile Investments

Eversheds Sutherland

Financial Services Consumer Panel

Graham Bentley Investment Intelligence

IM Asset Management

Implementation Taskforce for Growing a Culture of Social Impact Investing in the UK

Invesco Perpetual

Investment Adviser Association

JP Morgan Asset Management

London Stock Exchange Group

Margaret Beck

Max Griffith

McInroy & Wood

Morningstar

New City Initiative

PIMFA

Royal London Asset Management

Ruffer

ShareAction

SRI Services

St James's Place

The Investment Association

The Society of Pension Professionals

True Potential

UK Sustainable Investment and Finance Association

Which?

Annex 2

Abbreviations used in this paper

AFM	Authorised fund manager
AMMS	Asset Management Market Study
CMA	Competition and Markets Authority
COBS	Conduct of Business sourcebook
CP	Consultation Paper
CTI	Cost Transparency Initiative
ESG	Environmental, Social and Governance
EU	European Union
FCA	Financial Conduct Authority
FOWG	Fund Objectives Working Group
IA	Investment Association
IDWG	Institutional Disclosure Working Group
LGA	Local Government Association
MIR	Market Investigation Reference
NURS	Non-UCITS Retail Scheme
PLSA	Pensions and Lifetime Savings Association
PRIIPs	Packaged Retail and Insurance-based Investment Products
PRIIPs KID	PRIIPs Key Information Document
PS	Policy Statement
UCITS	Undertakings for Collective Investment in Transferable Securities
UCITS KIID	UCITS Key Investor Information Document

We have developed the policy in this Policy Statement in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

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Appendix 1

Made rules (legal instrument)

**COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK (MISCELLANEOUS
AMENDMENTS) INSTRUMENT 2019**

Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in or under:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
 - (a) section 137A (The FCA’s general rules);
 - (b) section 137R (Financial promotion rules);
 - (c) section 137T (General supplementary powers);
 - (d) section 139A (Power of the FCA to give guidance);
 - (e) section 247 (Trust scheme rules);
 - (f) section 248 (Scheme particulars rules);
 - (g) section 261I (Contractual scheme rules); and
 - (h) section 261J (Contractual scheme particulars rules);
 - (2) regulation 6(1) of the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228); and
 - (3) the other powers listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.
- B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

- C. (1) Part 1 of Annex B (COBS) to this instrument comes into force on 4 February 2019.
- (2) Annex A (Glossary), Part 2 of Annex B (COBS), and Part 1 of Annex C (COLL) to this instrument come into force on 7 May 2019.
- (3) Part 2 of Annex C (COLL) to this instrument comes into force on 7 August 2019.

Amendments to the Handbook

- D. The modules of the FCA Handbook listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex A

Conduct of Business sourcebook (COBS)	Annex B
Collective Investment Schemes sourcebook (COLL)	Annex C

Citation

- E. This instrument may be cited as the Collective Investment Schemes Sourcebook (Miscellaneous Amendments) Instrument 2019.

By order of the Board
24 January 2019

Annex A**Amendments to the Glossary of definitions**

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

Coming into force on 7 May 2019

comparator benchmark as defined in *COLL* 4.2.5R(3)(c-b)(iii).

constraining benchmark as defined in *COLL* 4.2.5R(3)(c-b)(ii).

target benchmark as defined in *COLL* 4.2.5R(3)(c-b)(i).

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text.

Part 1: Coming into force on 4 February 2019

4 Communicating with clients, including financial promotions

4.1 Application

Who? What?

...

4.1.7 G ...

What? Modification relating to the KII Regulation

4.1.7A R The rules in this chapter do not apply in relation to the form or content of a key investor information document, an EEA key investor information document or a NURS-KII document.

4.1.7B G (1) The KII Regulation specifies in an exhaustive manner the form and content of the key investor information document for a UCITS scheme.

(2) The form and content of a NURS-KII document is specified by COLL 4.7.3AR (Form and content of a NURS-KII document) and in COLL Appendix 2R (Modifications to the KII Regulation for KII-compliant NURS).

[**Note:** see article 3(1) of the *KII Regulation*]

...

Part 2: Coming into force on 7 May 2019

4 Communicating with clients, including financial promotions

...

4.5 Communicating with retail clients (non-MiFID provisions)

...

Authorised fund managers' communications in relation to benchmarks

- 4.5.12 R Subject to COBS 4.5.13R, an authorised fund manager must include in any communication about an authorised fund to which this section applies:
- (1) a short explanation, in terms consistent with the relevant prospectus, of the choice and use of every target benchmark, constraining benchmark or comparator benchmark used in relation to the scheme;
or
 - (2) where no target benchmark, constraining benchmark or comparator benchmark is referred to in the prospectus, a statement to that effect and a short explanation of how investors can assess the performance of the scheme.
- 4.5.13 R Where an authorised fund manager includes, in any communication about an authorised fund to which this section applies, an indication of past performance for any authorised fund it manages, it must (in addition to complying with COBS 4.6.2R where applicable):
- (1) include the corresponding past performance record of any target benchmark or constraining benchmark referred to in the prospectus of the scheme; and
 - (2) not include an indication of past performance for any index, indices or similar factor that is not referred to in the prospectus of the scheme.
- 4.5.14 R (1) Subject to paragraph (2), if a communication to which COBS 4.5.13R applies includes information comparing past performance of the scheme against one or more comparator benchmarks, the authorised fund manager must, for the period specified in paragraph (3) and in every subsequent communication it makes that is also subject to COBS 4.5.13R:
- (a) include a comparison against the same comparator benchmark or comparator benchmarks; and
 - (b) not include a comparison against any other benchmark.
- (2) Paragraph (1) does not apply if such a comparison would not be compliant with COBS 4.5.13R as a result of a change to the prospectus of the scheme.
- (3) The period specified for the purposes of paragraph (1) is:
- (a) twelve months after a one-off communication is made; or
 - (b) for as long as the communication remains available to the public in a durable medium and has not been superseded by a revised version.

4.5.15 **R** COBS 4.5.12R to COBS 4.5.14R do not apply in respect of any reference to a comparator benchmark that is not identified in the prospectus of the relevant scheme when that reference appears in a communication that is:

- (1) used exclusively in the course of a personal visit, telephone conversation or other interactive dialogue; or
- (2) in response to a specific unsolicited request by a client for past performance to be compared with a particular comparator benchmark.

...

TP 2 Other Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision : dates in force	Handbook provisions: coming into force
...					
2.- 1A	...				
<u>2.- 1B</u>	<u>COBS 4.5.12R to 4.5.15R</u>	R	<u>The rules specified in column (2) apply:</u>	<u>From 7 May 2019 to 7 August 2019</u>	<u>7 May 2019</u>
			(1) <u>from 7 May 2019 in respect of any authorised fund which is authorised on or after that date; and</u>		
			(2) <u>from 7 August 2019 in respect of any authorised fund which is authorised before 7 May 2019.</u>		
...					

Annex C

Amendments to the Collective Investment Schemes sourcebook (COLL)

In this Annex, underlining indicates new text and striking through indicates deleted text.

Part 1: Coming into force on 7 May 2019

4 Investor Relations

...

4.2 Pre-sale notifications

...

Table: contents of the prospectus

4.2.5 R This table belongs to *COLL* 4.2.2R (Publishing the prospectus).

...			
Investment objectives and policy			
3	The following particulars of the investment objectives and policy of the <i>authorised fund</i> :		
	...		
	(c)	...	
	(c-b)	<u>where:</u>	
		(i)	<u>a target for a <i>scheme's</i> performance has been set, or a payment out of <i>scheme property</i> is permitted, by reference to a comparison of one or more aspects of the <i>scheme property</i> or <i>price</i> with fluctuations in the value or price of an index or indices or any other similar factor (a "<i>target benchmark</i>"); or</u>
		(ii)	<u>without being a <i>target benchmark</i>, arrangements are in place in relation to the <i>scheme</i> according to which the composition of the portfolio of the <i>scheme</i> is, or is implied to be, constrained by reference to the value, the price or the components of an index or indices or any other similar factor (a "<i>constraining benchmark</i>"); or</u>
		(iii)	<u>without being a <i>target benchmark</i> or a <i>constraining benchmark</i>, the <i>scheme's</i></u>

		performance is compared against the value or price of an index or indices or any other similar factor (a “ <i>comparator benchmark</i> ”),
		a statement providing sufficient information for investors to understand the choice and use of any <i>target benchmark</i> , <i>constraining benchmark</i> or <i>comparator benchmark</i> in relation to the <i>scheme</i> ;
	(c-a)	where no <i>target benchmark</i> , <i>constraining benchmark</i> or <i>comparator benchmark</i> is used, a statement to that effect and an explanation of how investors can assess the performance of the <i>scheme</i> ;
	...	
	(o)	information concerning the historical performance of the <i>scheme</i> , comparing in particular its historical performance against each <i>target benchmark</i> and each <i>constraining benchmark</i> used in relation to the <i>scheme</i> , presented in accordance with COBS 4.6.2R (the rules on past performance);
	...	

...

Guidance on contents of the prospectus

4.2.6 G (1) ...

(1A) In relation to COLL 4.2.5R(3)(c-b), the prospectus might explain, if it is the case, that one index or factor may be used for both a *target benchmark* and a *constraining benchmark* in relation to the same *scheme*.

...

TP 1 Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provisions: coming into force
...					

<u>Amendments made by the Collective Investment Schemes Sourcebook (Miscellaneous Amendments) Instrument 2019</u>						
49	<u>COLL</u> 4.2.5R(3)(c-b), (c-a) and (o), and <u>COLL</u> 4.2.6G(1A)	R	The <i>rules and guidance</i> specified in column (2) apply:		From 7 May 2019 to 7 August 2019	7 May 2019
			(1)	from 7 May 2019 in respect of any <i>authorised fund</i> which is authorised on or after that date; and		
			(2)	from 7 August 2019 in respect of any <i>authorised fund</i> which is authorised before 7 May 2019.		
...						

Part 2: Coming into force on 7 August 2019

6 Operating duties and responsibilities

...

6.7 Payments

...

Performance fees

6.7.6 G ...

- (2) Any performance fee should be specified in the appropriate manner in the *prospectus* and should be consistent with *COLL* 6.7.4R. In determining whether the performance fee is consistent the *authorised fund manager* should have regard to factors such as:

- (a) ~~it should be calculated and paid after consideration of all other payments; [deleted]~~

...

...

6.7.6A R Any performance fee specified in the *prospectus* must be calculated on the basis of the *scheme's* performance after deduction of all other payments out of *scheme property*.

...

Appendix 2

Final non-Handbook guidance

The description of fund objectives and investment policies

February 2019

Introduction

1. One of the areas of concern identified in the asset management market study was the usefulness of fund objectives for investors. The market study found that it is difficult for investors to know what to expect from their fund and to assess whether or not their fund is performing against relevant objectives, including those set by the fund manager.
2. We consider that investors could benefit from greater clarity as well as being better able to compare objectives between similar funds.
3. We therefore set out the relevant provisions and how we expect these requirements might be complied with in practice.
4. This guidance applies to UK *authorised funds*.¹

Background

5. The objectives and investment policies of *authorised funds* must be provided in certain regulatory materials, and may also be provided in other documents that are subject to regulation. These may be categorised as long-form disclosures, short-form disclosures and marketing communications.

¹ Terms in italics in this document have the same meaning as in the FCA's Handbook Glossary.

Long-form disclosures

6. The *prospectus* of a UK *authorised fund* is required to state in detail what the investment objectives and policy of that fund are.²

Short-form disclosures

7. *UCITS schemes* are required to have a *key investor information document* (KIID).³ Providers of other investment products aimed at retail investors are likely to need to produce a *key information document* (KID) under the *PRIIPs Regulation* for each product.⁴ *Non-UCITS retail schemes* (NURS) may provide a document equivalent to the UCITS KIID, as an alternative to the KID.⁵ In this guidance, any reference to the UCITS KIID should be taken to include the NURS KII.
8. The UCITS KIID must contain a section on the objectives and investment policy of the fund.⁶ The PRIIPs KID must contain a section entitled 'what is this product?'⁷ This must describe the product's objectives and the means for achieving them.

Marketing communications

9. Other marketing communications, such as fund factsheets and other supporting literature, relating to a specific investment product are subject to the rules on communicating with clients in COBS 4. COBS 4 contains specific provisions in certain areas, for example on the disclosure of past performance, but does not contain specific rules on the content of disclosures of objectives and investment policies. At a high level, marketing communications must be fair, clear and not misleading. They are also required not to contradict or diminish the significance of information contained in the prospectus, KIID or KID.⁸

Existing obligations

Prospectus

10. The prospectus requirements are set out in COLL 4.2.5R (3). The prospectus disclosure must include, among other things:

The following particulars of the investment objectives and policy of the *authorised fund*:

- (a) the investment objectives, including its financial objectives;
- (b) the *authorised fund's* investment policy for achieving those investment objectives, including the general nature of the portfolio and, if appropriate, any intended specialisation;
- (c) an indication of any limitations on that investment policy;

² COLL 4.2.5R (3)

³ COLL 4.7.2R

⁴ Article 5 of PRIIPs Regulation (EU 1286/2014)

⁵ COLL 4.7.1R, COLL 4.7.1AG

⁶ COLL 4.7.2R (4)(b) and Article 7 of UCITS KII Regulation (EU 583/2010)

⁷ Article 8 of PRIIPs Regulation

⁸ PRIIPs Regulation and COBS 4.13.2R

(c-b) where:

- (i) a target for a *scheme's* performance has been set, or a payment out of *scheme property* is permitted, by reference to a comparison of one or more aspects of the *scheme property* or *price* with fluctuations in the value or *price* of an index or indices or any other similar factor (a "*target benchmark*"); or
- (ii) without being a *target benchmark*, arrangements are in place in relation to the *scheme* according to which the composition of the portfolio of the *scheme* is, or is implied to be, constrained by reference to the value, the *price* or the components of an index or indices or any other similar factor (a "*constraining benchmark*"); or
- (iii) without being a *target benchmark* or a *constraining benchmark*, the *scheme's* performance is compared against the value or *price* of an index or indices or any other similar factor (a "*comparator benchmark*"),

a statement providing sufficient information for investors to understand the choice and use of any *target benchmark*, *constraining benchmark* or *comparator benchmark* in relation to the *scheme*.

(c-a) where no *target benchmark*, *constraining benchmark* or *comparator benchmark* is used, a statement to that effect and an explanation of how investors can assess the performance of the *scheme*.

(ca) for an *authorised fund* that has indicated in its name, investment objectives or fund literature (including in any *financial promotions* for the fund), through use of descriptions such as 'absolute return', 'total return' or similar, an intention to deliver positive returns in all market conditions (and where there is no actual guarantee of such returns), additional statements in the *authorised fund's* investment objectives specifying:

- (i) that capital is in fact at risk;
- (ii) the investment period over which the *authorised fund* aims to achieve a positive return; and
- (iii) there is no guarantee that this will be achieved over that specific, or any, time period;

(d) the description of assets which the *capital property* may consist of;

(e) the proportion of the *capital property* which may consist of an asset of any description;

(l) where a *scheme* invests principally in *scheme units*, *deposits* or *derivatives*, or replicates an index in accordance with COLL 5.2.31R or COLL 5.6.23R (Schemes replicating an index), a prominent statement regarding this investment policy;

UCITS KIID

11. The UCITS KIID requirements are set out in the *KII Regulation* (Commission Regulation No (EU) 583/2010):⁹

Objectives and investment policy

Article 7

Specific contents of the description

1. The description contained in the 'Objectives and investment policy' section of the key investor information document shall cover those essential features of the UCITS about which an investor should be informed, even if these features do not form part of the description of objectives and investment policy in the prospectus, including:

- (a) the main categories of eligible financial instruments that are the object of investment;
- (b) the possibility that the investor may redeem units of UCITS on demand, qualifying that statement with an indication as to the frequency of dealing in units;
- (c) whether the UCITS has a particular target in relation to any industrial, geographic or other market sectors or specific classes of assets;
- (d) whether the UCITS allows for discretionary choices in regard to the particular investments that are to be made, and whether this approach includes or implies a reference to a benchmark and if so, which one;
- (e) whether dividend income is distributed or reinvested.

For the purposes of point (d), where a reference to a benchmark is implied, the degree of freedom available in relation to this benchmark shall be indicated, and where the UCITS has an index-tracking objective, this shall be stated.

2. The description referred to in paragraph 1 shall include the following information, so long as it is relevant:

- (a) where the UCITS invests in debt securities, an indication of whether they are issued by corporate bodies, governments or other entities, and, if applicable, any minimum rating requirements;
- (b) where the UCITS is a structured fund, an explanation in simple terms of all elements necessary for a correct understanding of the pay-off and the factors that are expected to determine performance, including references, if necessary, to the details on the algorithm and its workings which appear in the prospectus;
- (c) where the choice of assets is guided by specific criteria, an explanation of those criteria, such as 'growth', 'value' or 'high dividends';

⁹ Article 7 of UCITS KII Regulation. In the event that the Collective Investment Schemes (Amendment etc.) (EU Exit) Regulations 2019 are approved and come into force, references in article 7 to a "UCITS" will become references to a "UK UCITS" (see regulation 59(2)).

(d) where specific asset management techniques are used, which may include hedging, arbitrage or leverage, an explanation in simple terms of the factors that are expected to determine the performance of the UCITS;

(e) where the impact of portfolio transaction costs on returns is likely to be material due to the strategy adopted by the UCITS, a statement that this is the case, making it also clear that portfolio transaction costs are paid from the assets of the fund in addition to the charges set out in Section 3 of this Chapter;

(f) where a minimum recommended term for holding units in the UCITS is stated either in the prospectus or in any marketing documents, or where it is stated that a minimum holding period is an essential element of the investment strategy, a statement with the following wording:

'Recommendation: this fund may not be appropriate for investors who plan to withdraw their money within [period of time]'.

3. Information included under paragraphs 1 and 2 shall distinguish between the broad categories of investments as specified under paragraphs 1(a), (c) and 2(a) and the approach to these investments to be adopted by a management company as specified under paragraphs 1(d) and 2 (b), (c) and (d).

4. The 'Objectives and investment policy' section of the key investor information document may contain elements other than those listed in paragraph 2, including the description of the UCITS' investment strategy, where these elements are necessary to adequately describe the objectives and investment policy of the UCITS.

PRIIPs KID

12. The PRIIPs KID must contain the following information:¹⁰

(c) under a section titled 'What is this product?', the nature and main features of the PRIIP, including:

(i) the type of the PRIIP;

(ii) its objectives and the means for achieving them, in particular whether the objectives are achieved by means of direct or indirect exposure to the underlying investment assets, including a description of the underlying instruments or reference values, including a specification of the markets the PRIIP invests in, including, where applicable, specific environmental or social objectives targeted by the product, as well as how the return is determined;

(iii) a description of the type of retail investor to whom the PRIIP is intended to be marketed, in particular in terms of the ability to bear investment loss and the investment horizon;

13. This is further expanded in the PRIIPs Delegated Regulation as being:¹¹

Information stating the objectives of the PRIIP and the means for achieving those objectives in the section entitled 'What is this product?' of the key information document shall be summarised in a brief, clear and easily understandable manner. That information shall identify the main factors upon which return depends, the underlying investment

¹⁰ Article 8(3) of PRIIPs Regulation

¹¹ Article 2(2) of PRIIPs Delegated Regulation (EU 2017/653)

assets or reference values, and how the return is determined, as well as the relationship between the PRIIP's return and that of the underlying investment assets or reference values. That information shall reflect the relationship between the recommended holding period and the risk and reward profile of the PRIIP.

FCA expectations

Language requirements

14. Both the UCITS KIID and the PRIIPs KID are required to be written in language that communicates in a way that facilitates understanding of the information and that is clear, succinct and comprehensible.¹² The UCITS KIID must avoid the use of jargon and technical terms.¹³ The same requirement is implied of the PRIIPs KID.¹⁴
15. There are no explicit requirements about the style of language of the prospectus. The UCITS KIID and the PRIIPs KID require the information provided in them to be consistent with the information in the prospectus.¹⁵ This does not mean that the text must be identical to that in the prospectus.¹⁶ The Committee of European Securities Regulators (CESR), which was the predecessor to the European Securities and Markets Authority (ESMA), published a guide to clear language in the KIID.¹⁷

Description of factors that are not covered in the prospectus investment objectives and policy section

16. As noted above, there is no requirement for the text used in the prospectus to be identical to that used in the KIID or KID. Firms need to consider whether they should provide information in the KIID objectives and investment policy and the KID 'what is this product?' section which goes beyond what is set out in the prospectus.
17. Key information disclosure is intended to set out clearly and in terms understandable to retail investors what the overall aims of a fund are and how these objectives are to be achieved.¹⁸ It should also aid comparisons.¹⁹
18. The KIID section on objectives and investment policy must contain information on the broad categories of investments used and the approach to these investments.²⁰ There is a requirement to cover those essential features about which an investor should be informed, even if these features do not form part of the description of objectives and investment policy in the prospectus.²¹ It may contain other elements including the description of the investment strategy, where these elements are necessary to adequately describe the objectives and investment policy.²²
19. In practice, taking into consideration that the KIID should indicate to the investor what the overall aims of the fund are and how they are to be achieved, the FCA considers that it would generally be necessary for an adequate description of the objectives and investment policy to include relevant elements of the investment strategy. This description should explain those features of the investment strategy that are fundamental to how the product is managed, as illustrated by the following non-exhaustive examples. If it is not the manager's strategy to invest in a particular area where the investment policy permits investment, this should be made clear. If it is the manager's strategy to make specific use of one of the investment powers, for example around the use of derivatives, this should also be made clear. If the

¹² Article 5(1)(b) of UCITS KII Regulation and 6(4)(c) of PRIIPs Regulation

¹³ Article 5(1)(b) of UCITS KII Regulation

¹⁴ Recital 14 of PRIIPs Regulation

¹⁵ COLL 4.7.5R (3), Article 6(1) of PRIIPs Regulation

¹⁶ Recital 14 of PRIIPs Regulation, Article 2 of PRIIPs Delegated Regulation

¹⁷ CESR/10-1320, available at: https://www.esma.europa.eu/sites/default/files/library/2015/11/10_1320.pdf

¹⁸ Recital 5 of UCITS KII Regulation

¹⁹ Recital 4 of UCITS KII Regulation

²⁰ Article 7(3) of UCITS KII Regulation

²¹ Article 7(1) of UCITS KII Regulation

²² Article 7(4) of UCITS KII Regulation

manager's strategy is to focus on investments with particular characteristics, for example companies who are growing their business rapidly, this should be explained. If the manager's strategy is to be flexible about which opportunities they consider best, depending for example on their view of the market cycle, this should be made clear.

20. There are similar, though less detailed, provisions in the PRIIPs Regulation. The KID is intended to enable retail investors to understand and compare the key features and risks of a PRIIP.²³ The KID must include information about the PRIIP's objectives and its means for achieving them.²⁴
21. In practice, firms should consider how to describe the objectives, investment policy and investment strategy in a concise way and without using jargon, to enable a retail investor to understand the product.

Reference to a benchmark

22. In the UCITS KIID, firms must disclose whether the UCITS uses an approach that includes or implies a reference to a benchmark. The *KII Regulation* further requires that, where a reference to a benchmark is implied, the degree of freedom available in relation to the benchmark shall be indicated.²⁵
23. In practice, firms should consider whether their investment approach implies a reference to a benchmark. The FCA considers that where the fund is, in practice, constrained in how far its holdings can deviate from the weightings of a benchmark, this implies reference to a benchmark for the purposes of the *KII Regulation*. This includes situations where a fund is constrained in its portfolio construction relative to a benchmark.
24. The FCA also considers that, even where there is no explicit requirement for the manager to manage a fund's portfolio in line with a benchmark, there may be practical, internal restrictions within the firm which limit how far a fund can differ from the composition of a benchmark. Examples of such restrictions include, but are not limited to:
- the risk management process for the fund causing it to be monitored and controlled relative to a benchmark
 - the individuals managing the fund being remunerated based on its performance relative to a benchmark
 - the portfolio management system restricting transactions using hard or soft limits relative to a benchmark
25. Firms should assess whether such restrictions mean that the fund is in practice managed with reference to a benchmark. If so they should disclose this, along with the degree of freedom in relation to the benchmark, in the fund's KIID.
26. Where a fund has a *target benchmark* or a *constraining benchmark* we expect that this should be disclosed in the KIID.
27. The *KII Regulation* requires performance to be displayed against such benchmarks where used. Following on from the above, this is likely to mean that firms will need to provide

²³ Article 1 of PRIIPs Regulation

²⁴ Article 8 of PRIIPs Regulation

²⁵ Article 7(3) of KII Regulation

performance data in relation to each *target benchmark* and *constraining benchmark* they use.

28. When disclosing the degree of freedom, firms should use language that is clear, succinct and comprehensible and that avoids the use of jargon. They should also consider quantifying the degree of freedom.

Non-financial objectives

29. Sometimes funds set out non-financial objectives, for example environmental or social objectives, or state that they are aiming to achieve a non-financial return. We expect, if a fund has such objectives, that it will set them out in its prospectus and its KIID / KID.
30. Where a fund sets out objectives such as these, it must do so in a way that is fair, clear and not misleading. Firms that set out non-financial objectives for a fund should be clear about how they will measure whether those objectives are being met, and should provide ongoing information to investors.

