Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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By email: cp21-12@fca.org.uk

Dear Michael and Tom,

Financial Services Consumer Panel response to CP21/12: A new authorised fund regime for investing in long term assets

The Panel welcomes the proposals for a new category of authorised open-ended fund called the long-term asset fund (LTAF). We believe this will bring much needed clarity to funds that invest in longer term potentially illiquid assets, and where the value is purely driven by the underlying net asset value.

The consultation paper contains a range of issues, proposals and questions ranging from the technical operation of the product through to the consumer experience. We have focused our response on the proposition, distribution and consumer elements of the consultation.

As always, we champion clear, concise and easy-to-understand disclosure. This will be vital to consumers as they invest in these (and indeed any) funds. We see it as critical that the consumer understands the features, benefits and risks of any fund they are investing in and can judge how these align to their own personal needs and circumstances.

These disclosures should not be limited to the fund prospectus but should be obvious, clear and unambiguous in all promotional, pre-sales and sales literature and journeys - whether via IFAs or direct, whether sold through face to face, phone or online channels. Clear signposting will be key to this so that consumers know what this product is (and importantly isn't) right from the start of any consideration.

We believe that firms should be under a duty to act in the best interests of their customers. This duty would directly address the issues we raise in this response around disclosure, consumer understanding, provider and adviser responsibility and ensuring LTAF products are only invested in by those for which they are suitable.

Responses to the individual questions posed in the consultation are included in Annex A below.

Yours faithfully,

Wanda Goldwag
Chair, Financial Services Consumer Panel

Annex A – Answers to questions

Please note we have only included questions to which we are providing an answer.

Q2. Do you agree that clear disclosures and additional governance (as set out in 3.9-3.13 and 3.39-3.43), in addition to the existing rules, provide appropriate levels of protection for potential investors in an LTAF? If not, what alternative approach would you suggest?

We believe the clear disclosure is vital to support consumers as they invest in these funds. It is important that the consumer understands the dynamics and limitations of the fund they are investing in and how these meet their own personal needs. We would propose that such disclosures should not just be limited to the prospectus but should be clear and unambiguous in all promotional, pre-sales and sales literature and journeys. Firms should bear responsibility, via a duty to act in the best interests of their customers, for ensuring disclosures are clear and understandable for retail investors.

We welcome the use of the assessment of value reporting to give consumers an overview of the fund that goes beyond performance and cost metrics. We support the view that the requirements for this report are probably greater for LTAF funds than normal, liquid, investment funds.

We also support the approach that the responsibility for ensuring compliance with regulatory requirements must sit with an approved person, preferably the Chair of the Authorised Fund Manager (AFM) where possible. This person should be responsible, and accountable, not only for complying with requirements for product design and operation, but also for promotion and distribution, ensuring that the product is only promoted to those consumers for whom it is appropriate.

As part of any disclosure we believe it is important that charges, whether proportionate to value or performance related, are clear and easy to understand by the consumer. Furthermore, we believe disclosures should use examples and illustrations that are described in cash terms (pounds and pence) rather than just as percentages of the sum invested. It is well documented that many consumers struggle to understand percentages, and would better understand cash terms.

Finally, we would highlight to the FCA a potential unintended consequence (as we observe it) of successful disclosure and labelling. Consumers should view all investments as a medium to long term commitment, investing for at least a 5-year time horizon. It is important that the development, promotion and labelling of LTAF funds does not lead the average consumer to interpret that non-LTAF funds are short term (i.e. under 5 year) investment opportunities. The 'long term' element of the LTAF product refers to the relationship between the funds and the underlying asset and therefore a more limited redemption process. It mustn't create a false sense of long term vs short term (non-LTAF) investments with consumers.

Q5. Do you agree with our proposals to allow investments in LTAF for default arrangements of DC schemes if the conditions as outlined above are satisfied? If not, how would you change them to make them more workable for DC default arrangements?

Assuming all other proposals around governance, control, clarity of disclosure including fund operations and charges are met we have no objection to the proposal to allow investment in LTAF for default arrangements of DC schemes.

Q7. Do you agree that LTAFs should initially be treated as QIS for distribution purposes? Do you agree that LTAFs should be subject to the same guidance as

QIS on sophisticated and high net worth retail investors? If not, what alternative approach would you propose?

The Panel believes it is important that consumers investing in LTAF understand the complexities and restrictions of the funds. We believe the firm should bear the liability for ensuring that the fund is appropriate for the consumer and that the consumer fully understands the fund. Placing firms under a duty to act in the best interests of their customers would ensure that responsibility for suitability and consumer understanding is placed squarely on the firm, as opposed to potential investors.

We do not believe a self-certification route is appropriate as this may enable consumers to unwittingly invest in a fund that is not appropriate for them. We would therefore suggest that a different solution be used to ensure that distribution is better targeted and managed.

Q9. Do you think that the LTAF should be available for promotion more widely than to retail investors permitted to invest in NMPI? If not, why not?
AND
Q10: To what extent do you think the appropriateness assessment would help to protect retail investors in the LTAF?
AND
Q11: Do you think that the NRRS regime would work as a way of restricting investment in LTAFs, permitting them to be promoted to restricted investors? If not, why not?

<u>Distribution</u>

The Panel believes that the LTAF should be available to investors where it is clear that the consumer understands the fund, its liquidity (or lack thereof) and its limitations. The fund must also be viewed as being appropriate for the consumer. As we have said above, placing firms under a duty to act in the best interests of their customers will help ensure this is the case.

We would support the view that it is unlikely that widescale promotion of LTAF to all retail investors would be appropriate. Furthermore, we agree that LTAF should not be viewed as a non-complex financial instrument and as such distributors will need to conduct an appropriateness test for all prospective investors. We would stress that we do not believe that asking the consumer to self-certify that they are either a high net worth or a sophisticated investor is enough to satisfy the firm's responsibility to perform an appropriateness test.

We find the proposal to treat the LTAF in the same category as a non-readily realisable security to be an interesting, and potentially workable, solution. However, we would again see the responsibility for ensuring the appropriateness of the fund remaining with the firm, which should be able to demonstrate that both the appropriateness test and limitation on the amounts invested have been satisfied without the use of a consumer self-certification.

<u>Signposting</u>

The Panel believes it is important that consumers can easily identify the product they are about to purchase. This is an area of concern for LTAF products, as they are one of many different types of investment and the long-term nature of LTAF products could cause consumer detriment if not fully understood. Additionally, as the consultation proposes allowing a range of ways in which redemptions can be controlled, this further level of detail needs to be clear from the outset, in all promotional and sales materials, to enable consumers to assess if the product and its redemption processes and restrictions are right for them.

It will therefore be important to create the right language and terminology to clearly signpost LTAF products, and their distinctive redemption features, in a way that is clear, obvious and unmistakable. This needs to be clearly presented whether the consumer is accessing the fund via an Independent Financial Adviser (IFA) or direct/via a platform. It must enable the consumer to compare and contrast the different redemption approaches across funds as part of their investment decision making process.

Clear signposting is an important (but not the only) method to ensure that consumers understand the product they are investing in and we would hope that the FCA would test various approaches with consumers before settling on a preferred option.

Q12. Do you think that a minimum level of investment from professional clients would provide sufficient protection for retail investors?

Our concern with an approach that mandates a minimum level of investment from professional clients is that, whilst consumers may view this as a confirmation that professional investors have performed due diligence on the fund and take confidence from that, there is also the potential for this approach to create consumer harm.

There is likely to be an information and knowledge asymmetry between the professional investor (such as a large DC scheme) and the individual consumer investor. There is therefore the risk that the professional investors may decide to exit the fund, based on updated due diligence or knowledge, before individual investors are aware of any issues with the fund or that significant redemptions are about to take place. In such a scenario it could be the case that individual investors are left in the fund as performance deteriorates, waiting for the next opportunity to exit from the fund themselves.

Q14. What other options could we consider to make the promotion of the LTAF to retail clients more appropriate?
AND
Q15. Who else do you think the LTAF should be capable of being marketed to, and why? What are the barriers currently preventing this from happening?

The Panel believes that consumers should be able to access products such as the LTAF where it is appropriate for them and their needs and circumstances, and where they clearly understand the product, its benefits, the risks involved and any specific features such as limits on redemptions.

We would therefore support models where the firm promoting and/or distributing the product is responsible for ensuring that it is only promoted to consumers for whom it is appropriate and that any appropriateness test is conducted and recorded by the firm who remain responsible for its accuracy. This should be the case whether consumers access the product through an IFA or direct/via a platform.