

## UKLA Technical Note

### Non-equity retail prospectuses

Ref: UKLA / TN / 632.1 Consultation

Prospectus Directive, Article 5.1; Prospectus Directive, Recital 16; Prospectus Directive Regulation, Annex XII, 4.1.2.; PD Amending Directive, Recital 3; Regulation (EC) No 809/2004, Recital 14.

#### **Non-equity retail prospectuses: ensuring they are “easily analysable and comprehensible”**

Article 5.1 of the Prospectus Directive requires all prospectuses, including a non-equity retail prospectus, to be ‘easily analysable and comprehensible’.

This technical note sets out some of the key aspects that issuers should consider when preparing a retail prospectus, in order that such documents are ‘easily analysable and comprehensible’ to a retail audience.<sup>1</sup> Please note that this technical note does not provide issuers with an exhaustive list of issues and they should consider the nature of the securities and the prospectus as a whole when drafting non-equity retail prospectuses.

#### **When is this guidance relevant?**

We consider prospectuses relating to non-equity securities that have a denomination of less than €100,000 to be ‘retail’ prospectuses. This is consistent with the distinction between wholesale and retail securities made in the Prospectus Directive Amending Directive.<sup>2</sup>

This guidance is therefore relevant to retail denominated debt prospectuses and base prospectuses and retail denominated prospectuses and base prospectuses for structured products. This is the case even in circumstances where it is intended that a retail denominated prospectus will be used to issue securities to wholesale or exempt investors.

#### **How do I make my prospectus easily analysable and comprehensible to retail investors?**

Outlined below are a number of key areas that we suggest issuers consider to make a retail prospectus easily analysable and comprehensible to investors. Other considerations may also be relevant, depending on the nature of the individual securities.

##### **a) Language**

A prospectus should be written in a style that is easily analysable and comprehensible to a retail investor. This means the prospectus should not be written in a legal style, nor should it place excessive reliance on the use of defined terms, technical language or market jargon. Where

<sup>1</sup> See Article 5.1 of the PD and Recital 16 of the PD, which states that it is appropriate to take account of the various categories of investors and their level of expertise.  
<sup>2</sup> See PD Amending Directive, Recital 3 and Regulation (EC) No 809/2004, Recital 14.

such language is used it should be clearly explained in each section of the prospectus where this language is used.

We recognise that the Terms and Conditions sections of retail securities may be directly reproduced from legal documents containing legal language. For this reason, we do not propose that the language in the Terms and Conditions section be presented in the 'easily analysable and comprehensible' language highlighted in this technical note.

### **b) Navigating the prospectus**

Where a prospectus relates to more than one type of security, comprehensibility is greatly enhanced by including clear instructions about which sections of the document apply to a particular security. Issuers may wish to consider the use of 'sign-posting' to enable an investor to navigate through the prospectus to find the sections relevant to a particular security. This will be especially helpful where different types of securities may be offered or where certain investment features may or may not apply. A short section at the beginning of the document that clearly explains key aspects of the document could be included detailing, for example:

- a description of the type of securities that the prospectus relates to,
- a 'How do I use this prospectus?' section, and/or
- a description of the type of underlying asset to which the securities may be linked.

### **c) Calculating the return on maturity or interest payment where the maturity or interest payment is determined by a derivative component.**

Prospectuses relating to structured products and to securities where the coupon is determined by a derivative component must give 'a clear and comprehensive explanation...of how the value of the investment is affected by the value of the underlying instrument(s).'<sup>3</sup>

The description of an investor's return should be presented without using complicated technical jargon or complex mathematical formulae. Use examples to explain complex securities, especially where various separate pay-out features or underlying linked terms may need to be explained to investors, either separately or together, producing a series of different outcomes. However, a simple equation or narrative describing the yield in the case of less complex securities may also be acceptable.

### **d) FAQs**

FAQs are helpful, but are not essential. Although we do not require retail prospectuses to include FAQs, they are one method that can be used to make prospectuses easily analysable and comprehensible.

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<sup>3</sup> Prospectus Directive Regulation, Annex XII.4.1.2 and Annex V.4.7.

### **e) Explaining bond holder protections and bond features**

Retail investors are may not be nor knowledgeable of the risks that can be built into bonds which, when combined with the credit risk of the issuer, will not only determine the credit rating of the bond but will, when combined with the prevailing interest rates, also determine the coupon.

For a retail investor to understand why a bond pays a relatively high coupon in a low interest rate environment, the prospectus should clearly identify the features and risks associated with that bond. The prospectus should also clearly explain how the protections and rights that have been built into the bond might work in a default scenario. For example, if the bonds are secured, there should be clear explanation of what this means and the process that needs to be undertaken before bond holders will receive repayment of all or part of their principal. Similarly, if bond holders will be structurally subordinated, then this fact and its significance should be explained, so that holders are aware that they will rank behind other creditors.

To ensure that retail investors fully understand the features, risks, protections and rights associated with a bond, this information should be presented in an easily analysable and comprehensible format, either through:

- a clear narrative, or
- the use of a diagram with accompanying text separately from the terms and conditions of the bond.