

UCITS Advertising and Retail Investors

The advertising of UCITS is facing a double challenge.

It must be commercially efficient. It must also be informative, i.e. clear, accurate and not misleading.

Recent case law in France has put these familiar requirements in a new perspective. In a widely reported case¹ in June 2008, the court has, for the first time, imposed liability on a bank for publishing marketing material to retail investors which was over-optimistic.

The rationale behind this decision is the reasserted requirement that UCITS advertising must be consistent with the proposed investment and must mention the less favorable characteristics and the risks attached to the product which could be the downside of the advertised advantages. Specific legislation relating to the financial sector, but also a general "*obligation d'information*", or duty to provide accurate information on the part of the bank, were relied on in the decision.

The legal basis above broadly echoes the Luxembourg legal framework. The Luxembourg financial sector may thus not ignore the recent judicial trend in France against inappropriate advertising.

What lessons may hence be drawn?

1. A prospectus is not an absolute protection

The marketing material at the origin of the new case law emphasized, as often occurs, the positive aspects of the investment, whereas the risks were detailed in the prospectus. The advertising material did not contradict as such the provisions of the prospectus, and the retail investor had expressly acknowledged having received the prospectus. The liability of the bank was however triggered. Accordingly, professionals must consider the validity of the advertisement independently from that of the prospectus. A prospectus does not operate as a shield allowing wide freedom in terms of the content of marketing materials.

2. Advantages/risk balance

All marketing materials (leaflets, slides, etc...) need to mention both the advantages and risks of investing in UCITS. French case law and the French regulator (AMF)² have eloquently provided clear guidelines on this requirement, which has its Luxembourg equivalent in the rules of conduct of the financial sector.

The following examples are not to be considered as balanced advertising: advertisements employing a language enhancing a feeling of security (such as "there is no reason to worry"), affirming certitudes ("performance assured"), or summing up features on purpose to obtain an attractive catch copy ("take full advantage of the performance of the stock market!"), without presenting in parallel the risks attached to the investment (e.g. by mentioning that the performance available will be the average performance of the market over several years).

¹ CCass. Ch.commerciale 24 juin 2008(Aubin / Caisse d'épargne et de prévoyance Ile de France PARIS

² Guide to sound practices in drafting marketing documents published by the AMF, updated in July 2009

3. Formulation of wording and form of advertisement

The risks attached to a potential investment must not only be mentioned in the advertisement, they must also be sufficiently highlighted and, according to the AMF, must not be presented in an opaque manner, e.g. through the use of a mathematic formula or highly technical wording which is not adapted to the targeted customers. The use of ambiguous wording, the common understanding of which does not match the actual features of the product, or the presentation of the risks involved as an advantage (e.g. praising a target of 10% growth, while the average index reaches 15%), may also result in the advertisement breaching the rules.

Beware of the form, i.e. where risks are mentioned in footnotes or in small characters while favorable features are in the main text, in capital letters, or the reader is directed to another document for details of the risks. There is no need however to provide all necessary information in each document. The level of information is to be adapted to the nature of the material used and succinct messages may be dispatched if the balance principle is respected.

With these recent developments, France is seen as a precursor in the protection of retail investors regarding UCITS advertising. In 2009, the FSA also imposed a fine upon City Gate for approving financial advertising designed to encourage investment in a scheme without ensuring and monitoring that the advertising in question was clear and not misleading. More generally, the overall trend of European legislation is to seek an enhanced standard of information and transparency, as illustrated notably by the MiFID Directive. Further developments in this area are emerging with the UCITS IV Directive (still to be implemented), which aims, through the Key Investment Documentation, to ensure effective communication in an accessible and comparable manner. The KID will however not make up for non-compliant advertising and the principles above will remain more than ever accurate.

Marie-Béatrice Noble / Valentine Oblin

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Contacts

Marie-Béatrice Noble

Partner
T: +352 26 48 42 35 07
noble@mnks.com

Valentine Oblin

Manager
T: +352 26 48 42 35 42
oblin@mnks.com

Noble & Scheidecker

398, route d'Esch
L-1471 Luxembourg
T: +352 26 48 42 1
F: +352 26 48 42 35 00
www.mnks.com