Appendix 2

Literature Survey in regards CIS Disclosures at the Point of Sale

Literature/research submitted

This note draws together findings and issues from the research or surveys submitted by members of TCSC3 and TCSC5.

In particular, this note draws on:

- The report submitted by AMF, *Investigation of investment information and management processes and analysis of disclosure documents for retail investors* (TNS Sofres, November 2006) (AMF Study];
- The market research report submitted by ASIC, *Developing health warnings about investment risks in prospectuses* (TNS Sofres, February 2002) (ASIC Study);
- The consumer research series submitted by the UK FSA[1];
- Consumer testing done on behalf of the US Securities and Exchange Commission[2];
- A research study (Canadian Study) commissioned by the Task Force to Modernize Securities Legislation in Canada, entitled *How are Investment Decisions Made*[3];
- Hong Kong SFC *Survey on Engagement of Investment Advisers* (Sept. 2006) (SFC Study);
- An Investment Company Institute (ICI) research report on *Understanding Investor Preferences for Mutual Fund Information* (2006) (ICI Study); and
- Report prepared for the Investment Funds Institute of Canada (IFIC) by Pollara, Inc.,

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1 *Consumer Research* series; studies consulted are cited individually below.

2 The Commission retained Siegel & Gale, LLC and Gelb Consulting Group, Inc. (S&G) to help develop and test model disclosure forms that would effectively convey information to investors. See Siegel & Gale, LLC/Gelb Consulting Group, Inc., *Results of In-Depth Investor Interviews Regarding Proposed Mutual Fund Sales Fee and Conflict of Interest Disclosure Forms: Report to the Securities and Exchange Commission*, (November 4, 2004) and *Supplemental Report to the Securities and Exchange Commission* (November 29, 2004) [together, SG1]. The report is available at http://www.sec.gov/rules/proposed/s70604/rep110404.pdf and the supplemental report is available at http://www.sec.gov/rules/proposed/s70604/suprep010705.pdf. We also received additional information through continued testing of potential disclosure forms, as well as consumer testing of oral disclosures. See Siegel & Gale, LLC/Gelb Consulting Group, Inc., *Results of Investor Interviews to Test and Refine Point of Sale Disclosure Forms* (May 31, 2005) [SG2] (available at http://www.sec.gov/rules/proposed/s70604/siegel053105.pdf) and *Results of Investor Interviews to Test Oral Point of Sale Disclosure* (June 1, 2005) (available at http://www.sec.gov/rules/proposed/s70604/supprpt060105.pdf) [SG3]. See also Low & Associates, Inc., *Results of Focus Groups with Individual Investors to Test Proposed Rules 15c2-2 and 15c2-3,* (April 2004) [Low].

3 Richard Deaves, Catherine Dine, William Horton (May 24, 2006).

entitled *Canadian Investors' Perceptions of Mutual Funds and the Mutual Fund Industry* (2006) (IFIC Report).

1. Key Findings and Common Themes

The key findings in the research group together around common themes, which we have used to organise the findings in this summary. Some key points (which are outlined in more detail below) include:

- *What do consumers want?* Investment returns are a key focus for many consumers, along with information about risks, costs (including fund fees and expenses), and intermediary conflicts of interest;

- *What ways of presenting information do consumers prefer?* Generally, consumers prefer short, well-laid out and plainly worded documents, without 'legalese' or marketing material. Although open to electronic disclosure, most investors appear to continue to prefer to obtain fund information in paper form (particularly mutual fund investors) or from a professional financial adviser, rather than online, prior to purchasing. Oral disclosure can also be an important means of providing investors with information that is integrated into the sales process;

- *How do consumers make decisions?* Consumers can rely on a range of information sources other than official disclosure documents when making investment decisions, including a significant reliance on the advice of others, including salespersons. However, other factors play an important role including emotion (e.g., intuition), personality (e.g., overconfidence),[4] and "representativeness" (i.e., a tendency to be inappropriately influenced by past performance;

- *What are the limitations or biases with consumer decision-making?* Consumers can exhibit a range of biases when making decisions, such as wrongly discounting information, or overly relying on poorly understood or misunderstood disclosures; and

- *What are the implications for consumer behaviour?* Consumers do not necessarily alter their behaviour or understanding, even where exposed to better disclosure documents.

Research needs to be placed in a context that the baseline for financial capability can be rather low. For example, according to a research project conducted recently by the UK FSA,[5] many consumers have a poor understanding of financial services and products, including an understanding of remuneration arrangements, or the nature of different asset classes and fund types and their associated risks.[6] The low levels of consumer understanding stand as a key

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4 For example, the IFIC Report (p. 17) found that almost all of the surveyed Canadian investors in mutual funds say that they felt comfortable that they had the right information to make an informed decision about investing in mutual funds.

5 See http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf.

6 Studies suggest that when terms or concepts may be unfamiliar to investors, it may be necessary to include additional explanatory text in disclosure documents [SG1 p. 6].

driver of much of the research, including the AMF, ASIC, Canadian and UK FSA research submitted.

A further general point is that some of the research submitted focuses on "unpacking" the preferences of investors using qualitative techniques followed, in some cases, by additional quantitative research to provide some statistically relevant support. In general terms, qualitative research techniques are particularly suited to exploring preferences. The conclusions can contribute to the fine-tuning of disclosure documents. However, the methodological limitations of such research can make it difficult to generalise findings, or to make assumptions as to the likely impact of particular documents on consumer behaviour. We return to this issue under Section V below.

2. What do consumers want to know when purchasing investment products

Given this limitation, evidence nonetheless suggests that a key starting point for consumers when looking at investment products is information about benefits, risks, costs (including fund expenses and fees as well as sales-related costs), historical performance, and conflicts of interest. Investors seem to be asking the following: What might he/she get back from an investment? What could impact on the investment? What conflicts may be influencing an intermediary's recommendation? And, how much of the investment could be lost to charges and commissions?

The AMF noted that consumers most want to receive a description of the features of the product providing information about risk, expected return/loss and fees and that they are less interested in many other details, such as the description of typical profile or even the rack record of the fund. Research by the UK FSA has also shown that consumers focus on information about investment returns or performance more generally.[7]

Consumers do not, however, only focus on benefits. They also want to know about risks and guarantees, and any limits on guarantees.[8] Investors typically, regardless of their level of sophistication, wish to understand the extent to they can rely on an investment.[9] For example, the investors surveyed in the SFC Study indicated that that three most important things they *should know* before investing are (1) capital risk; (2) expected return and calculation method; and (3) historical performance.[10]

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7 [AMF Study], p. 41; FSA: *Informed decisions? How consumers use Key Features:a synthesis of research on the use of product information at the point of sale* CR5 (November 2000), p. 16 ('What consumers want') [FSA: Informed Decisions].

8 Even though UK FSA evidence regarding financial capabilities suggests a low level of understanding of the nature of different asset classes and their performance characteristics. See [FSA: Informed Decisions]; FSA: *The development of more effective product disclosure* CR18, (March 2003) [FSA: More Effective Disclosure]; FSA: *Investment Disclosure Research*, CR55, (November 2006) [FSA: Investment Disclosure Research]. See also http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf

9 Low capabilities of course can have the effect of reducing consumers' ability to grasp the limits of guarantees; evidence form the UK FSA suggests many investors take products contained in a particular life policy tax wrapper in the UK to be guaranteed even when they are clearly stated to not be so. See [FSA: Investment Disclosure Research], p.3.

10 Page 3.

In addition, investors also have expressed an interest in product costs.[11] For example, the ICI Study found that investors are most interested in a fund's fees and expenses and its historical performance.[12] The significance of product costs is particularly illustrated by the fact that salespersons pay special attention to costs. ASIC notes that "when presented with a series of prospectuses for examination in the group discussion, most advisers opened straight to the fees and charges."[13]

Personalized information (e.g., a fee estimate specific to their purchase amount), may be a particularly helpful way to communicate cost information.[14]

ASIC, AMF, Canadian and UK FSA research all suggested questions of trust can be a key factor in consumer behaviour, in relation to which (as we will see later) consumers often focus on intuition. UK FSA research suggests that by comparison, cost and remuneration information can seem of secondary importance to the investor.[15] While some evidence suggests that the investor may be primarily seeking reassurance in regards the trust they are already potentially extending to the advisor, and so may discount disclosure evidence which is contrary to this,[16] other studies indicate that investors are likely largely unaware of the incentives their market intermediary may receive for recommending one fund over another and find such information useful.[17]

The timing of the disclosure can be key to its effect. Investors want information at a time that is useful to their investment decision.[18]

3. What designs and formats are effective in achieving consumer engagement

Qualitative research techniques are also particularly suited to teasing out the elements of the design of disclosure information that are particularly effective from the perspective of the consumer.

Key messages repeated throughout the literature are that consumers prefer documents which

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11 See [AMF Study], p. 40; [FSA: Informed Decisions], p.16; [Low] p. 3.; [SG1] p. 6. Of note, many investors prefer "complete" disclosure of fees paid rather than disclosure only of some fees (e.g., sales or other fees paid to their intermediary). [SG1], p. 7. This suggests that if only some fees are set forth, disclosure should emphasize that other fees will be charged, and if possible state the potential amount (e.g. "up to $100 per year"). [SG1], p. 7; [SG2], p. 5.

12 Page 1-2.

13 The ASIC Study.

14 See [SG1], p. 4.

15 FSA: unpublished research, *Depolarisation Disclosure, Qualitative Research*, BMRB, 2006. [FSA: Depolarisation Disclosure]. FSA: *Polarisation: Consumer Research*, (January, 2002), p. 31 [FSA: Polarisation]

16 [FSA: Polarisation]. Other factors that have been emphasised by investors in UK FSA research [FSA: Depolarisation Disclosure] include: information on the range of products, information about the advisor and their status (e.g. their 'independence').

17 [Low].

18 [Low], p. 3

are:

- short;
- well presented and laid out;
- plainly and clearly worded;
- focused on the information they believe they need; and[19]
- the ICI Study noted that mutual fund shareholders look for concise investment information and, where possible, graphic presentations.[20]

Design techniques may be used to improve the extent to which a document engages consumers. However, making a document engaging is only part of the larger picture: other points to consider include the relative prioritisation of different messages within a document, [21]and the extent to which a document is able to create a particular impression (e.g., that it is neutral or trustworthy, or that it ranks or prioritises key messages in the appropriate way).

Detailed design factors include:

- the use of colour and visual cues to enliven documents and call investors' attention to particular pieces of information;
- the effective use of space to make documents easier to follow and less overwhelming; and
- the deployment of well-paced and logically sequences of information.[22]

Readability can be seen as a function of all of these elements of layout. The prioritisation of information and use of focus within a document can also help impart key messages unambiguously.[23]

The overall 'tone' of a document also matters. For instance, AMF and S&G note a consumer preference for documents that are honest and accessible.[24] (This preference is tempered

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19 For instance, ASIC noted that "in judging the merit of a prospectus, investors look for clarity – the prospectus had to be simple to read." One way to accomplish this may be to provide disclosure in a "layered" manner, where brief disclosure is provided initially with more detailed information available either upon request or accessible on the Internet.

20 Page 2.

21 See, e.g., [SG3 Summary]; [SG2], p. 2 (the order of information presented can aid or hinder comprehension; for example, investors were better able to recall certain information when it was made at the beginning of a conversation).

22 [SG1], pp. 2-4.

23 [AMF Study], p.41. Of note, some studies suggest that investors find "yes/no" questions easy to comprehend, and the information useful even when "no" was the appropriate answer.

24 [AMF Study], p. 35-36.

however by a desire that the documents are not off-putting and that their accessibility does not lead them to become untrustworthy.) Statements regarding where investors could find more information have been viewed as enhancing the overall credibility of the information disclosed, even when the investor indicated little likelihood of accessing the additional information.[25] The research notes that consumers find neutral documents reassuring, and feel that they offer a degree or element of 'explanation'. The researchers concluded that "the main challenge is to strike a balance between the need to be accessible and non-technical and the need to be trustworthy".[26] Readers were hostile to anything which came across as advertising, and preferred documents which felt official.[27]

UK FSA and US SEC research also amplifies and supports these points, including the preference for clear and straightforward presentation, the use of plain language, and a preference for short documents.[28] This is supported by the Canadian Study as well.[29]

The UK FSA research has also drawn out the extent to which consumers often are more comfortable with presentational techniques with which they are familiar, such as the use of tabular question and answer sections. For instance, when examining different ways of presenting information about projected returns on long term investments in funds, the UK FSA found that many respondents tended to be more confused by, or take the wrong message from, unfamiliar presentational techniques (showing richer and more sophisticated information using putatively easier to understand grasp graphical techniques) when compared with the use of familiar tabular presentational styles.[30] This is confirmed by the Canadian Study.[31]

A further point worth drawing out is that research suggests that different ways of showing similar information can create different degrees of reliance or focus on the information amongst consumers. For instance, UK FSA research into the presentation of past performance information suggests presentation can impact on a users' emotional response to and reliance on information (for instance, through the use of figures showing cumulative cash gains or losses).[32]

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25 [SG1], p. 8

26 [AMF Study], p. 46,

27 Many investors in one study interpreted their signature on a form negatively, and believed their signature established a contractual agreement to the fees stated on the form. [SG2], p. 3.

28 These points recur across UK FSA research; see, in particular, [FSA: Informed Decisions], [FSA: More Effective Disclosure] and FSA: *KeyFacts Quick Guide - research findings* CR41, (July 2005) [FSA: KeyFacts Quick Guide].

29 The Canadian Study noted that "[w]hen information overload occurs, there is a tendency for retail investors to simply tune out and not try to process the information at all". Page 263.

30 UK FSA unpublished research by Synovate, *Projections research: Reviewing projections Key Facts documents* 2005 [FSA: Synovate]. Importantly, the effectiveness of different presentational techniques can be significantly segmented in demographic terms, with respondents having divergent needs. For instance, respondents can split into those who respond well to text and figures, and those who prefer graphical presentations.

31 The Canadian Study refers to this as *familiarity bias* (which in turn is related to the *status quo bias).* This is the degree of comfort that people have in the familiar. This leads to placing a greater value on what is known. Page 254.

32 FSA: *Standardisation of past performance*, CR21, (May 2003) [FSA: Standardisation of Past Performance].

Putting these points another way, it is clear consumers respond to devices which place information in a context with which they are familiar or which imparts impressions of trustworthiness or reliability. For instance, a common theme explored in the ASIC, AMF and UK FSA research, is the perceptions respondents have of the regulator along with the regulator's role in relation to disclosure information.

Key tensions concern the extent to which information provided is seen as 'legalese' (consumers often express frustration in the face of 'small print'), or as something that can be relied on and which has some form of 'independence'.[33] These points relate to wider points in regards 'branding,' which we return to below.

One study indicated that information disclosed orally can be useful and easy to understand.[34] Investors commented that such disclosure could facilitate discussions with their salesperson. Nonetheless, investors who received oral disclosure still expressed a preference for access to additional information in digital or printed form. This particular study also indicates that the order of the information presented can aid or hinder comprehension (for example, investors were better able to recall information about conflicts of interest when the disclosure was made at the beginning of the conversation).

More generally with regard to format, the Canadian Study observed that investors still generally access disclosure information in paper form, and that mutual fund investors had lower levels of electronic information usage and comfort levels.[35] Notwithstanding the tremendous growth in the use of the Internet, the ICI Study found that only 30% of recent fund investors prefer to obtain mutual fund information online rather than by mail or in-person from professional advisors.[36]

4. What factors do consumers use in decision making

While messages about consumer preferences and the information they believe they should be receiving appear relatively consistent and clear, understanding the actual information consumers' use when decision-making can be more complicated.

In thinking about this, we need to also take into account the wider context impacting on particular investment decisions, such as the consumer's reliance on the advice of others, whether or not they are buying directly, or their use of other sources of information (such as promotional material, press coverage, information available through their employer, or 'word-of-mouth').[37] As ASIC research suggested, these other factors can have a significant effect on investor' actual reliance on documents: "Investors' use of prospectuses appeared casual at best, with no real consensus on the worth of a prospectus document as a stand-alone

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33 See [ASIC Study], p. 21; [AMF Study], pp. 35-46; more generally, [FSA: Informed Decisions]; [FSA: More Effective Disclosure]; [FSA: KeyFacts Quick Guide]; see also [SG1], p. 5 (direct and colloquial language was found to be effective while jargon, and legal terms were not).

34 [SG3 Summary], [SG2] p. 2.

35 Page 286.

36 Page 33.

37 See for a wide ranging discussion of the information that investors use, FSA: *Better informed consumers*, CR1, April 2000, and [FSA: Informed Decisions].

source".[38] Indeed, the Canadian Study found that for investors, including mutual fund investors, the prospectus is one of the least used sources of information.[39] The ICI Study went further and stated that "most shareholders do not consult fund prospectuses or annual reports."[40] It is true that 63% of the investors surveyed as part of the SFC Study "looked at the product's offering documents or fact sheets,"[41] but this does not necessarily mean that they reviewed prospectuses in a meaningful way.

The Canadian Study also found that, with regard to mutual fund transactions, the key driver in decision making is the financial advisor recommendation, followed by past performance.[42] This is consistent with the SFC Study, which found that 72% of the surveyed investors relied on their investment adviser's verbal recommendations or financial plans in making their investment decisions,[43] and with the ICI Study ("shareholders usually turn to professional financial advisers for information before purchasing shares").[44]

The key information investors seek that we noted above – information about historical performance, risk, and cost (particularly in the mutual fund context) – remains important, but investors may find apparent answers to their questions by a variety of means. The ASIC research noted that "typically, after investigating a prospectus, the investor would take their decision back to the adviser to attempt to gauge the adviser's recommendation".[45] This reliance on others is particularly the case where the investor rates themselves as poorly equipped to make investment decisions.

Nonetheless, even for investors who indicated a heavy reliance on their salesperson's recommendations, and commented they would be likely to continue to depend on those recommendations, information regarding costs and conflicts of interest was considered useful as an educational tool and viewed as a prompt for them to ask their salesperson for more information.[46]

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38 [ASIC study], p. 19.]. Even where investors appear to use disclosure documents, evidence suggests that they may particularly focus on messages regarding the risk–reward balance of the particular investment. However, the focus can be significantly segmented demographically. Some more sophisticated investors may focus more directly on price measures, for instance as a key determinant of investment outcomes once portfolio diversification has been addressed. See [FSA: Informed decisions]. [FSA: Synovate] examined respondents' use of projection information according to the 'sophistication' of the respondent, and saw significant differences. [ASIC Study] distinguished throughout between 'direct' and 'indirect' investors. Also see FSA: UCITS: charges disclosure – presenting product charges to customers, CR34, (April 2005).

39 Page 286-7.

40 Page 2.

41 Page 17.

42 Page 288. The IFIC Report (p. 18-19) likewise found that the following were the top three factors that surveyed mutual fund investors considered most seriously before they last invested in mutual funds: the advisors' opinion; the risks associated with investing in the fund; and the fund's past performance compared to other funds in its category.

43 Page 17.

44 Page 9.

45 [ASIC Study], p. 20.

46 [SG1], p. 2.

The mechanisms that sustain or undermine the investor's trust in the person who is advising them then become significant, which we will discuss in the next section.

Other elements also come to the fore in decision-making where the investor feels they lack understanding. For instance, consumers can turn to intuition: AMF, ASIC, the Canadian Study and UK FSA all highlight perceptions by some consumers that their 'gut-feeling' about an investment is the key factor they rely on.[47]

The evidence also suggests that one particularly important factor is brand-identity and familiarity, which can be used by consumers as proxies for the reliability and trustworthiness of an investment proposition.

For instance, UK FSA evidence notes that consumers use their experience of brand in non-investment areas and apply it when making investment decisions – and this brings with it well known effects such as the impact of brand-loyalty.[48] ASIC note that consumers often assume that general firm behaviour around brands can be assumed to apply to investment firms – for instance, that the value of a brand to firms means they will generally not take actions likely to damage the brand.[49]

5. What are the limitations of consumer decision making/biases

In considering the limitations of consumer decision-making, the low levels of financial capability are a key theme, as discussed above. Low basic understanding lays a key part of the basis for consumers to misunderstanding key messages or disregard important information.[50]

Other kinds of bias or limitation also can be found. The framing and positioning of information can be very important in terms of the messages consumers of the information take away. For instance, we have already touched on evidence that information will strike consumers differently depending on whether it is contained within marketing documents or standalone, or how the information is introduced or positioned, e.g., through a regulatory message, other branding, or by an intermediary/ other third party.

Consumers can exhibit biases where they are interpreting and assessing information: for instance, UK FSA research and the Canadian Study suggest that consumers can be overly optimistic about future returns;[51] AMF and ASIC research both also note the extent to which consumers can overly find some information off-putting, as they may exhibit a (patchy) aversion to risk which concentrates on certain elements of risk (e.g. risk to capital) at the

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47 [AMF Study], p. 37; [ASIC: TNS Sofres], p. 19; [FSA: Depolarisation Disclosure]; [Canadian Study], p. 278 (24% of respondents indicated that "gut feeling or intuition" was important to them).

48 See for instance [FSA: Informed Decisions], p. 20.

49 [ASIC Study], p. 19.

50 Some information was deemed useful only when accompanied by information that could allow the information to be put into context.

51 Indeed, the Canadian Study suggests that investors inappropriately rely on past fund performance. Page 279.

expense of others (e.g. inflation).[52]

Although work in this area is only now being fully developed, other early indications for the UK FSA include the capacity of some information to become 'false focal points' which is readily misinterpreted by consumers.[53] This can be particularly acute where low levels of financial capability are common. The false focal points typically cluster around the information about benefits, risks and costs that the investor is most seeking. The desire for answers can itself drive the misreading, as consumers seek to fit information into their existing understandings.[54]

For instance, research into the use of information about future benefits by investors has shown there to be number of common problems.[55] These can be characterised as errors in understanding the limitations of information being provided; thus, despite textual messages, consumers can focus on the figures they are most seeking, and disregard the caveats to these. Though figures might be presented relatively clearly as only suggestive, and in no way guaranteed, respondents will overly rely on them.

These tendencies to misunderstand or misinterpret can therefore make it difficult to provide simple messages which include key information the investor is seeking in ways which are not going to be misleading. The UK FSA research into past performance data and work on the presentation of risk offers a case in point in regards this sort of issue.[56]

In relation to advice, the relationship between the investor and the advisor raises the interesting question of the role of trust. Trust is used by consumers where they need to rely on others. In these cases, consumers will typically rely on a full range of social tools for assessing the situation: they may summarise the conclusions of this process in terms of a 'gut-feeling' they have in regards the other person. Obviously, for advisors able to create the right social environment and impression, this can offer a significant opportunity to create a bond with the investor to promote increased sales. As ASIC noted 'on the whole, in front of the client, the prospectus was used simply as a sales tool.' For the client however,

> "there was a tacit statement of trust in the adviser's recommendations. The legitimacy of the advice given was generated through an assumption that the adviser spends considerably more time investigating the strength of various investments than the individual investor would be able to do."[57]

This brings to the fore necessary limitations in the capacity of consumers to properly adjudge the credibility or reliability of expertise in regards the advisor. The consumer understands that they cannot unaided make a decision; however, they may not have a ready way to

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52 For a summary, see FSA: *Informing Consumers: a review of product information at the point of sale,* Discussion Paper (Nov 2000), Annex B, p. 3 (for the fuller report see [FSA: Informed Decisions]).

53 See [FSA: Standardisation of Past Performance] and [FSA: Synovate].

54 [Canadian Study], page 254.

55 [FSA: Synovate], and [FSA: Informed Decision], pp. 15-19.

56 [FSA: Standardisation of Past Performance] and FSA: *Consumer understanding of financial risk* CR 33, (November 2004).

57 [ASIC Study], p. 17.

evaluate their relationship with their advisor and the appropriate degree of reliance on that advisor. Low financial capabilities can amplify the problems here, as consumers only poorly understand the conflicts of interest which may impact on their advisor. The psychology and sociology of trust is certainly more complicated than can be analysed here.[58]

1. On questions of trust, AMF research indicated that more than two thirds of retail investors questioned said it was important or vital to have access to an official approved document before investing. However, the AMF research also raised some concerns regarding the role of the regulator. One half of the respondents thought the regulators role entailed ensuring that the investment is financially advantageous for the investor, especially when a prospectus is approved by the Securities regulator.

2. The SFC Study did look into the issue of investor evaluation of their investment advisors.[59] 88% of the surveyed investors were satisfied with their investment advisor services. Investors were least satisfied with their investment advisor's fees and charges.[60]

6. How does the format and content of information have an impact on actual consumer behaviour and outcomes?

The research outlined in the above overview focussed on exploring consumer preferences, using techniques such as focus groups and other interview based surveys. It did not explore issues such as:

- How far changes in either the format or content of information change consumer's actual understanding of products or their purchasing behaviour; and

- How the disclosures work in a real world environment where many other influences may be at work.

Research within this area has, understandably, been limited, a reflection of methodological, legal and practical difficulties. The UK FSA has, as part of its cost benefit work surrounding the development of a new disclosure regime in 2005-2006 (refs inset), explored techniques to test the effectiveness of proposed changes to the disclosure regime for investment products.[61] Prior to introducing the regime, it wished to test whether the new approach yielded materially different consumer (outcomes and) understanding. The results were quite stark:

- Although consumers confirmed their preference for the new material, it did not materially increase their understanding of the product or its risk; and

- Even without rule changes, firms could achieve a lot by presenting the material more clearly.

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58 [FSA: Depolarisation Disclosure]; [FSA: Polarisation].

59 Page 20.

60 Page 21.

61 The FSA developed a "Quick Guide" for investment products to replace its Key Features regime, on the basis of focus group research.

The work did not identify why there was this apparent mismatch of preferences and understanding, although limitations in financial capability (mentioned above) were clearly a significant contributor. It also has limitations as a measure of real behavioural change since it was not conducted in the environment of a "real sale", where many other influences are likely to impact on both consumer and advisor behaviour. The UK FSA is attempting to trial live testing for oral disclosures and investment product intermediary disclosure later this year, but the methodology is still being developed.

Conclusions

The research suggests the following key themes:

- Consumers do not understand many key messages about charges, remuneration, conflicts of interest, and fund risks and features based on current disclosure regimes, and will commonly simply follow the advice of others.

- Investors would like the format and content of disclosures to be carefully designed to promote accessibility and readability.

- When designing an appropriate point of sale disclosure, regulators may need to:

    a) Consider investor frames of reference, biases and emotions in order to enhance the likelihood of accurate investor comprehension of material facts;

    b) Take into account the overall impact of information and the different contexts in which it may be used; and

    c) Consider how different forms of point of sale disclosure (e.g., documents or oral disclosure) may generate a meaningful and positive behavioural change.