

## EFAMA's comments on the ESAs' Joint Consultation Paper PRIIPs Key Information Document [JC 2015 073]

### *Introductory comments*

After having looked extensively at the Level-2 work done by the ESAs, EFAMA<sup>1</sup> comes to the unfortunate conclusion that, due to the very technical nature of the underlying methodologies and calculations, there will not be enough time for market participants to fully implement the PRIIP KID by 31 December 2016.

This challenge is most relevant for the providers of PRIIPs falling directly under the PRIIPs Regulation (including retail AIFs in some Member States) and hence facing a factual ban on distribution from 1 January 2017 in case of their inability to provide a PRIIP KID to retail investors. It is also of utmost importance to UCITS which – while being exempted by the Level-1 Regulation – might be required to provide “PRIIPs-like” information to manufacturers which use these funds as underlyings for their products (such as insurance-based investment products). Taking this into consideration, we urge the ESAs to consider in their upcoming discussions with the Commission and the co-legislator that a delay of one calendar year (for the date of entry into application) is foreseen to allow for proper implementation of the PRIIPs Regulation<sup>2</sup>.

The existing time constraints are also fully apparent in the work of the ESAs which, in spite of their considerable efforts, struggle to finalise their respective workloads before the end of the obviously unrealistic deadlines. We notice this shortage of time in a number of conflicting and contradicting technical rules (e.g. on the calculation of risk), the introduction of completely new concepts at this late stage (e.g. arrival price for the calculation of transactions costs) and the general aim to include as many highly technical elements as possible in the draft RTS.

The latter is most apparent when comparing the current proposal to the existing UCITS KIID rules which provide a more general framework at Level-2, but subsequently identify technical details through Level-3 guidelines and Level-4 Q&As. It appears that the impending coming-into-force of the

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<sup>1</sup> EFAMA is the representative association for the European investment management industry. EFAMA represents through its 26 member associations and 61 corporate members almost EUR 19 trillion in assets under management of which EUR 12.1 trillion managed by 55,700 investment funds at end September 2015. Just over 29,500 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 26,100 funds composed of AIFs (Alternative Investment Funds). For more information about EFAMA, please visit [www.efama.org](http://www.efama.org).

<sup>2</sup> This request for a delay of one calendar year also reflects on the implementation time that was granted by the co-legislators when enacting the UCITS KIID. At the time, a one-year period between the date of final adoption/publication of the UCITS KIID format and the date of compliance was provided to the UCITS fund management companies in scope.

Regulation is the main reason behind the ESAs not following this tried and tested model, as any provisions included into Level-3 guidelines would require further public consultation and thus risk derailing the finalisation of the overall framework. This is particularly important as these technical aspects will need to be refined over time and need a more flexible updating process than can be accommodated in a Level-2 Regulation.

Keeping these considerations in mind but being of the clear opinion that further consultations on the more technical aspects are undoubtedly needed, we request that certain provisions of the draft RTS be included in Level-3 or Level-4 measures. These include most of the annexes, but most specifically the risk calculation (calculations for market risk and credit risk) and cost calculation methodologies (i.e. table for standardised transaction costs).

From a legal perspective, we strongly oppose the ESAs' view that would require multi-option product (MOPs) to provide information on underlying investment options through a PRIIP KID. This clearly oversteps the Level-1 Regulation which simply requires "generic description" of these underlying investment options which can undoubtedly be satisfied by providing a UCITS KIID to investors (for those funds already required to produce a UCITS KIID).

On a technical level, we strongly disagree with the proposal on the PRIIP risk categories and the subsequent Market Risk Measure. We are categorically against combining into the same Class-7 MRM PRIIPs that may lose the investor more than the money invested (i.e. creating additional payment liabilities) and other types of PRIIPs with high volatility. This would create the perception for retail investors that potentially losing much of your invested money is equally as risky as investing into a PRIIP that creates additional payment liabilities beyond the initially invested amount. Furthermore, we are strongly against the methodology prescribed to calculate potential transaction costs for a number of reasons, such as the inclusion of market movements (which is at odds with MiFID II) as well as the clear lack of market data available to make those calculations. The proposed standardised transaction cost table should also be used for all transactions where data cannot be calculated (not just for new PRIIPs) in order to calculate implicit transaction costs and should furthermore be updated and maintained by ESMA on a much more frequent basis than is proposed in order to allow accurate cost comparison among all PRIIPs.

Lastly, the format of the standardised questionnaire inhibits respondents from providing the ESAs with feedback to the draft RTS beyond the questions specifically posed. This submission therefore makes full use of the ESAs' invitation to respond to all aspects of the RTS (page 3) and provides the ESAs with our additional comments on these important sections of the consultation separate to our answers below.

### *Comprehension alert*

**Question 1**

*Would you see merit in the ESAs clarifying further the criteria set out in Recital 18 mentioned above by way of guidelines?*

The criteria for the comprehension alert in Recital 18 are clearly linked to the definition of complex and non-complex financial instruments described under MiFID II (Art. 25(4)) as well as complex and non-complex insurance-based investment products under IDD (Draft IDD Art. 30(3)). This means that any PRIIPs considered as non-complex in either MiFID II or IDD should not require a comprehension alert. By corollary, the need for a comprehension alert needs to be considered only for those PRIIPs considered complex under MiFID or IDD.

We believe that no further clarification around Recital 18 is required at this time. We are aware that the Commission is invited to conduct a “general survey of the operation of the comprehension alert” as part of its review of the Regulation by 31 December 2018. This survey and the Commission’s review will provide further insights into whether further criteria on the comprehension alert are needed in the future.

### *Standardised amounts used as a basis for calculations*

#### **Question 2**

- (i) *Would you agree with the assumptions used for the proposed default amounts? Are you of the opinion that these prescribed amounts should be amended? If yes, how and why?*
- (ii) *Would you favour an approach in which the prescribed standardised amount is the default option, unless the PRIIP has a known required investment amount and price which can be used instead?*

The same default amounts should be used for all types of PRIIPs. Having different default amounts for different PRIIP types will hinder comparability for retail investors. We have no strong view whether this default amount should be €1,000 or €10,000, as long as it is one and the same for all PRIIPs. The same logic should apply to PRIIPs denominated in non-Euro, whereas the factor for the default amount should be either 1,000 or 10,000.

Furthermore, to ensure comparability between all types of investment products, PRIIPs with a higher or prescribed investment amount should use the standard default amount (i.e. either €1,000 or €10,000) for the purposes of the performance scenarios and costs calculation. The minimum or prescribed investment amount should be disclosed clearly to the investor within the KID to inform him/her that only this (minimum) amount can be invested.

### *Risk and Reward: Application of methodology*

#### **Question 3**

*For PRIIPs that fall into category II and for which the Cornish Fisher expansion is used as a methodology to compute the VaR equivalent Volatility do you think a bootstrapping approach should be used instead? Please explain the reasons for your opinion?*

First, it is unclear into which categories of UCITS and AIFs fall – II, III or V. This is due to the conflicting and imprecise wording of Annex II, which should be redrafted and simplified. The determination of

which PRIIPs fall into which category is of utmost importance, as the MRM calculation is dependent on the PRIIPs categorisation. Even though the calculation formulas for category II PRIIPs had already been declared erroneous in the open hearing on 9 December 2015, an errata was published only on 5 January 2016. This confusion has seriously impeded the practical analysis and assessment of the calculation methodology. Discussions on the formula need to continue also among the expert group in order to eliminate any errors and to allow the stakeholders for a renewed assessment. Otherwise, no final evaluation of methodology or comparison between Category II and III PRIIPs will be possible.

Notwithstanding the confusing text, we agree that the Cornish Fisher expansion is an appropriate methodology to be applied for Category II PRIIPs.

Preliminary calculations using the corrected Cornish Fisher expansion for Category II PRIIPs show that many UCITS tend to end up in the same two MRM risk bucket as the currently used 7-scale SRRI. We thus question whether the implementation costs of a new methodology for UCITS and AIFs (already using the UCITS KIID) are justified, as applying the new risk methodology still arrives at the same market risk indicator.

We must highlight that a PRIIP's MRM must always be comparable to the risk level of other PRIIPs which would not be the case. We are categorically against combining PRIIPs where the investor may lose more than the money invested (i.e. creating additional payment liabilities) and other types of PRIIPs with high volatility into the same Class-7 MRM. This would create the perception for retail investors that potentially losing much of your invested money is equally as risky as investing into a PRIIP that creates additional payment liabilities beyond the initially invested amount. **We therefore strongly request the creation of a new Class-8 MRM exclusively for PRIIPs where the maximum loss can exceed the money initially invested.**

Additionally, under the ESAs' proposal most equity funds will end up with a MRM of 6 to 7, while PRIIPs invested in illiquid assets will be qualitatively assigned an MRM of 5 at the most, regardless of whether or not they provide adequate risk diversification or a limitation on leverage. We deem this outcome inappropriate and it will not provide investors with a clear and comparable assessment of risk associated with PRIIPs investments. The ESAs must be careful not to create room for product arbitrage which might under- or overestimate risk(s) of certain PRIIPs, thus potentially impairing comparability and undermining effective protection of European investors.

Also, for PRIIPs investing in illiquid assets (Category V), if product manufacturers are confident have sufficiently accurate data available to them to calculate their MRM according to Category II or III, they should be allowed to do so and refer only to Annex II para. 14 in case of insufficient data.

Furthermore, we are categorically against using "bootstrapping" for Category II PRIIPs, as preliminary calculations show that "Cornish Fisher" calculations provide almost the same results and this additional exercise provides no cost-benefit advantage, to investors nor to manufacturers. This is even more the case because the majority of funds will fall into only two numbers of the seven-point scale. During the open-hearing in Frankfurt the ESAs admitted that the results of "Cornish Fisher" and "bootstrapping"

were comparable. **We therefore strongly suggest to use the Cornish Fisher expansion for all Category II PRIIPs.**

Lastly, we observe that the methodology proposed as well as the standardised table for new funds proposed in para. 13 of Annex II omits to consider the position of multi-asset, absolute return, life-cycle PRIIPs, etc. For example, mixed/flexible/multi-asset funds fall would be systematically categorised as MRM class-6, which is highly questionable. The same seems to be the case for all structured PRIIPs which fall into the same MRM class and do not take into account the level of capital protection.

### *Risk and Reward: Confidence level*

#### **Question 4**

*Would you favour a different confidence interval to compute the VaR? If so, please explain which confidence interval you would use and state your reasons why.*

We agree with the ESAs' proposal to use a confidence interval of 97.5%.

However, we believe that PRIIPs manufacturers should be allowed to choose the confidence interval within an imposed range from 95% to 99% when calculating internally and then rescaling to a standardised confidence interval of 97.5%. This approach is in use through the current UCITS CESR/ESMA guidelines when calculating the global risk VaR. It allows product manufactures to align this particular risk calculation with other risk calculation measures already applied internally, thus making these calculations less resource intensive.

### *Risk and Reward: Guarantee schemes*

#### **Question 5**

*Are you of the view that the existence of a compensation or guarantee scheme should be taken into account in the credit risk assessment of a PRIIP? And if you agree, how would you propose to do so?*

We are of the strong view that the existence of a compensation or guarantee scheme should not alter the credit risk assessment of an individual PRIIP (and thus its manufacturer). The KID has been designed to ensure that retail investors are being made aware of potential benefits and risks of a PRIIP. While it may make sense to highlight the existence of such schemes to investors<sup>3</sup>, it must be ensured that these compensation or guarantee schemes are seen as a measure of last resort and not as some additional benefit that lower the credit risk of a PRIIP. Systematically lowering (or even nullifying) the credit risk for a PRIIP that is connected to a (national) compensation or guarantee schemes would even create additional systemic risks, as it would allow PRIIPs with a high credit risk the strong benefit of a compensation scheme and therefore appear as risky as PRIIPs with a lower credit risk.

<sup>3</sup> This disclosure has to be kept within the context of the DGS Directive (2014/49/EU) which ensure that guarantee schemes shall not be used for advertisement purposes (Art. 16(5)).

Moreover, the level of potential additional protection through such schemes is capped at a certain maximum amount per financial institution and per individual investor (and is contingent on further factors such as the period of assertion, entitlement, etc.). Therefore, including the fact of such a scheme in the credit assessment of an individual PRIIP could mislead investors to believe that investing larger amount is equally protected.

Please also consider our reply to Q10 for more comments on the proposed credit risk assessment for UCITS and AIFs.

### *Risk and Reward: Summary Risk Indicator (SRI) risk class*

#### **Question 6**

*Would you favour PRIIP manufacturers having the option to voluntarily increase the disclosed SRI? In which circumstances? Would such an approach entail unintended consequences?*

We believe that an increase of the SRI should be allowed in a number of circumstances, such as, but not limited to, (i) increasing the SRI by one risk step in case the calculated SRI is oscillating between two risk buckets and (ii) setting the SRI by default at 7 if the manufacturer considers the product to be of high risk in any circumstances.<sup>4</sup>

Furthermore with regards to oscillation between two risk buckets, an important provision in the UCITS SRRI is missing, namely "[t]he synthetic risk and reward indicator shall be revised if the relevant volatility of the UCITS has fallen outside the bucket corresponding to its previous risk category on each weekly or monthly data reference point over the preceding 4 months."<sup>5</sup> This provision should be included for PRIIPs with regards to the migration rules for the MRM. However, given the widely diverse population of PRIIPs relative to UCITS, we suggest that this period should be lengthened to one calendar year. This lengthened period is necessary as we expect the currently proposed PRIIPs' SRI to change much more frequently than the current UCITS SRRI.

### *Risk and Reward: Aggregated scale of the SRI (Market Risk Measure & Credit Risk Measure)*

#### **Question 7**

*Do you agree with an adjustment of the credit risk for the tenor, and how would you propose to make such an adjustment?*

We agree with an adjustment of the credit risk for the tenor, as the calculation for market risk is also reflecting the higher risk for longer holding period for long term investments (e.g. higher discount for bonds with longer maturity). Not reflecting the tenor in the credit risk would give the false impression to retail investors that the credit risk of an obligor is the same, no matter the actual holding period of a PRIIP.

<sup>4</sup> For example, this option may be useful for a number balanced funds or CPPI funds whose risk exposure may be sensibly augmented compared to the recent past.

<sup>5</sup> CESR's guidelines on the methodology for the calculation of the synthetic risk and reward indicator in the Key Investor Information Document;

As stated in previous replies, we believe the credit risk scale should also contain seven risk classes to coincide with the 7-scale Market Risk Measure. This should allow aggregation that is less biased towards MRM as currently proposed.

### *Risk and Reward: Aggregated scale of the SRI (Market Risk Measure & Credit Risk Measure)*

#### **Question 8**

*Do you agree with the scales of the classes MRM, CRM and SRI? If not, please specify your alternative proposal and include your reasoning.*

We deeply regret the ESAs' decision to aggregate market risk and credit risk into a single risk indicator. In line with our previous replies, we are extremely sceptical about the supposed value of such an artificial aggregation and thus the added benefit (if any) for retail investors. Indeed, we are very concerned that it will mislead or perpetuate a lack of understanding among investors.

Second, please also consider our strong reservations against combining PRIIPs that may lose the investor more than the money invested (i.e. creating additional payment liabilities) and other types of PRIIPs with high volatility into the same Class-7 MRM. We therefore strongly request the creation of a new Class-8 MRM exclusively to PRIIPs where the maximum loss can exceed the money initially invested. Please see our further comments in Q3.

Third, as already mentioned in our answer to Q3, we are also concerned that the current scales do not allow for proper MRM comparability between all types of PRIIPs. Under the current proposal, most equity funds will end up with a MRM of 6 to 7, while PRIIPs invested in illiquid assets will be assigned an MRM of (at most) 5, regardless of the degree of diversification or the level of leverage applied.

Generally speaking, it seems that when aggregating market and credit risk into the summary risk indicator, credit risk is underrepresented. We believe that MRM and CRM should carry equal weightings. In any case, **we are strictly against the proposed alternative to restrict the number of credit risk classes to five, therefore further underweighting credit risk and creating a more unlevel playing field between different types of PRIIPs** which would further bias against market risk in favour of credit risk in the overall risk aggregation.

### *Risk and Reward: Capital protection and tenor*

#### **Question 9**

*Are you of the opinion that for PRIIPs that offer a capital protection during their whole lifespan and can be redeemed against their initial investment at any time over the life of the PRIIP a qualitatively assessment and automatic allocation to MRM class 1 should be permitted?*

*Are you of the opinion that the criteria of the 5 year tenor is relevant, irrespective of the redemption characteristics?*

We agree with the proposed automatic allocation of a PRIIP to MRM class 1 when there is full (100%) capital protection. However, we seek further clarity on the definition of "capital protection" and that it may not correspond to a legally enforceable commitment.

We are nevertheless categorically against extending a PRIIP's automatic assessment to MRM class 1 beyond a five-year tenor. It is imperative that retail investors are not left under the impression that receiving back the initial investment amount after a long investment period is the same as a risk-less investment. Developments in terms of inflation and general market circumstances are generally not predictable over the longer term. While the amount lost to inflation (when receiving back the initial investment amount) may not be that relevant in the first five years (at least in the current low-interest rate environment<sup>6</sup>), this effect is exaggerated after a holding period of more than five years.

### *Risk and Reward: Credit risk mitigating circumstances*

#### **Question 10**

*Are you aware of other circumstances in which the credit risk assessment should be assumed to be mitigated? If so, please explain why and to what degree it should be assumed to be mitigated?*

We are not aware of any circumstances in which the credit risk assessment should be assumed to be mitigated. The Solvency II Directive, CRD IV/CRR and the Bank Recovery and Resolution Directive (among others) are merely tools to mitigate systemic risk by large institutions on the financial sector to reduce the need of public interventions for these institutions in times of great financial distress. These directives merely provide for further systemic risk buffers, but do not make these institutions infallible, thus rendering null and void the need to assess credit risk for PRIIPs connected to these institutions. In a worst case scenario, assuming that any PRIIP issued by institutions falling under such schemes would categorically lower their credit risk, would make these products seem less risky than comparable products. This, in turn, could even increase the systemic risk to the financial markets as a whole, which should not be the effect of the PRIIP KID Level-2 measures.

We welcome the ESAs' statement on page 40 (para. 54 of Annex II to section 3) confirming that, in principle, credit risk shall not be assessed on AIFs or UCITS. This is correct because investment funds do not expose investors to manufacturers' credit risk because they are not on the balance sheet and very few have credit risk to guarantors.

We believe the cases outlined by the ESAs in relation to para. 55 of Annex II to section 3 (on page 40, completed by explanatory text on page 76), in which credit risk is still meant to be considered for funds, should be discarded, because all potential credit risk arising within a fund's portfolio impacts the fund's NAV and thus is already covered by its market risk. As a result, we think that for all calculations of the SRI, a fund's credit risk should always be considered as being CR1.

As to the explanatory text for para. 55 lit. (c), the ESAs may consider lowering the credit assessment

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<sup>6</sup> For example, if you apply a 5% inflation rate over a five-year period, the effect is that the value of a €1,000 investment (assuming no growth) in real terms is €783.53 which represents an effective loss of in excess of 20%.

by one credit risk class in the case of a third-party guarantee of the payoff, as it provides a dual layer of protection of investment through the fund's investment strategy and the third party-guarantee).

Finally, the absence of a guarantee scheme should not make funds be disregarded in comparison to other products. Funds, whose investments are insolvency remote, should instead be able to highlight the role of the depositary in the section "What happens if [the name of the PRIIP's manufacturer] is unable to pay?". All assets which the depositary holds in custody must be subject to adequate segregation and the depositary's safekeeping duties are detailed by EU and national law.

### *Risk and Reward: Credit risk look through approach*

#### **Question 11**

*Do you think that the look through approach to the assessment of credit risk for a PRIIP packaged into another PRIIP is appropriate?*

A look-through approach to the assessment of credit risk may be necessary if packaging into another PRIIP is used to escape the assessment of credit risk of the effective underlying. However, it should not generally apply in the case of PRIIPs investing in other PRIIPs or into other underlying instruments as suggested in para. 55 (d) of Annex II. The credit or counterparty risk involved with such investments should be considered part of the market risk as is the case for other investments in underlying assets and indeed, will be captured by the historical volatility data or performance simulations relevant for establishing the MRM category.

There is an important link between this proposal and that for MOPs. Many MOPs are insurance products with the underlying investment options being investment funds. Funds do not generally bear CR but insurance products do. The generic KID for the MOP should therefore show the effect of the CR of the insurer, otherwise MOPs produced by insurers with very different credit ratings will appear to carry the same overall risk for consumers.

### *Risk and Reward: Currency Risk*

#### **Question 12**

*Do you think the risk indicator should take into account currency risk when there is a difference between the currency of the PRIIP and the national currency of the investor targeted by the PRIIP manufacturer, even though this risk is not intrinsic to the PRIIP itself, but relates to the typical situation of the targeted investor?*

Generally speaking, the KID is meant to describe the overall characteristics of a PRIIP and not factor in the aspects of the individual investor such as, but not limited to national currency, risk appetite or tax situation. Therefore, the approach chosen to showcase the potential currency risk (when there is a difference between the currency of the PRIIP and the national currency of the investor targeted by the PRIIP manufacturer) should be disclosed from the point of view of the PRIIP and not that of the individual investor.

The currently proposed narrative for PRIIPs “denominated in a currency other than the legal tender in the Member State where the product is being marketed” will in effect require a separate KID for every country the PRIIP is being marketed into in case it diverges from the retail investor’s currency, which will inhibit cross-border distribution in the EU single market. We propose a more generic statement in element c of Annexes III’s Appendix 1 that should avoid such duplications, but still sufficiently alert the retail investor to the currency risk.

*[Where applicable: c] The money you get back is in [insert currency]. If your country has another currency, this means that the value of this product to you also depends on the exchange rate between [currency of product] and the currency of your country.*

### **Risk and Reward: Products with higher risk during the life of the product than at maturity**

#### **Question 13**

*Are you of the opinion that the current Consultation Paper sufficiently addresses this issue? Do you it is made sufficiently clear that the value of a PRIIP could be significantly less compared to the guaranteed value during the life of the PRIIP? Several alternatives are analysed in the Impact Assessment under policy option 5: do you see any additional analysis for these assessment?*

Yes, we think the Consultation Paper addresses the issue sufficiently.

The SRI should clearly indicate that it is computed on the assumption that the investor keeps the PRIIP until maturity, and therefore that it does not cover risk associated with early redemptions by investors or secondary market transactions. A warning should be required for capital guaranteed PRIIPs, stating that the value of the PRIIP could be significantly lower than the guaranteed value during the life of the PRIIP due to market and liquidity risk and fluctuations of market prices (as covered in element I on page 50).

### **Risk and Reward: Performance fees in the performance scenarios**

#### **Question 14**

*Do you agree to use the performance fee, as prescribed in the cost section, as a basis for the calculations in the performance section (i.e. calculate the return of the benchmark for the moderate scenario in such a way that the return generates the performance fee as prescribed in the cost section)? Do you agree the same benchmark return should be used for calculating performance fees for the unfavourable and favourable scenarios, or would you propose another approach, for instance automatically setting the performance fees to zero for the unfavourable scenario? Please justify your proposal.*

We severely regret that the PRIIP KID will not allow past performance to be shown. Our experience with the UCITS KIID shows that investors wish to see the product’s history of returns (where there is

one). They have the benefit of being based on facts, and give a useful indication of the way in which a fund is run<sup>7</sup>.

We believe that the ESAs have misinterpreted the Level-1 Regulation, requiring future performance scenarios for all types of PRIIPs, whereas it is clear from the text that “appropriate” performance scenarios may also entail showcasing past performance data where suitable. This is fully in line with the UCITS KIID framework which considers that only structured UCITS should provide performance scenarios in order to showcase their non-linear pay-off profiles to investors. **Consequently, non-structured funds should be allowed to present their past performance data as appropriate performance scenarios in the PRIIP KID.**

If the ESAs still consider the use of performance scenarios for all types of PRIIPs, we would generally agree to use the performance fee, as prescribed in the cost section, as a basis for the calculations in the performance section. Nonetheless, we have the following comments:

In principle, a performance fee applies when superior performance arises and it may be appropriate to demonstrate it kicks in only in the favourable scenario. The moderate scenario should represent achieving the target performance, whereby no “over” performance arises and the unfavourable scenario should represent underperformance of the target.

Also, the ESAs are considering to use the past performance of the last five years as the benchmark (Annex VI, para. 9, page 63) of the moderate scenario. This requires PRIIP manufacturers to define “unfavourable” and “favourable”, which are completely different from historic performance and may lead to the wrong assumptions about performances in these two scenarios. Furthermore, such an approach would also assume that the past performance of the last five years’ could always be considered a moderate performance, which may not be the case. For example, if a PRIIP substantially outperformed its benchmark in the past five years, this outperformance would now be considered as the normally expected return under the moderate scenario. It appears too short-sighted to make the choice of relevant scenarios entirely dependent on the past results in terms of performance fees. Hence, it should be left to the discretion of the product provider whether the previous performance results which generated the performance fee are presented as a moderate or a favourable scenario depending on the extent of the achieved outperformance and the underlying development of the markets.

Moreover, fund providers should also have the discretion to assume different benchmark returns for different scenarios in order to avoid overly positive performance presentation where there has been outstanding market performance in the preceding years. For instance, under the approach proposed by the ESAs, equity funds which succeeded to beat their respective benchmarks would have been required to make assumptions on their performance on the basis of very positive market

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<sup>7</sup> Even while past performance may not be shown in the KID, it is imperative that UCITS Management Companies and AIFMs are allowed to continue its use in their funds’ fact sheets. This is essential, as at least one NCA has used the wording in the UCITS Directive (Directive 2009/65/EC, Article 77) to require firms to alter their cost disclosures in general marketing, including factsheets, meaning they could similarly use the wording in Article 9 of the PRIIP KID Regulation to require performance scenarios to be used instead of past performance..

developments in the years 2003-2007, even though market prospects had dramatically changed and the fund managers knew that past performance figures would not be even remotely achievable in the near future. In this case, and assuming that other funds would follow the general line of illustrating performance on the basis of reasonable and conservative assumptions about future market conditions, it might even be that the ESAs would have created an unjustified bias in favour of funds charging performance fees by requiring excessively positive performance presentation on the basis of historical data.

In any event, the approach presuming that the return of the benchmark will remain stable for all scenarios should be clearly limited to events where a benchmark is being used as a determinant for performance fee calculation. Such an assumption implies that a fund is able to generate performance that is detached from the relevant market developments which is certainly not true in every case.

Moreover, with regards to the comparison of different types of PRIIPs, we disagree with the statement in para. 3 of Annex V (page 54), which stipulates that “in cases where products are considered to be illiquid according to Annex II part 5 paragraph 76, no information on the performance scenarios for the interim periods is required.” We consider that only PRIIPs with no disinvestment possibility before the recommended holding period (RHP) should be allowed to provide only one, performance scenario for the RHP. This is important as some illiquid PRIIPs do indeed offer disinvestment opportunity before the recommended holding period, but at additional costs and/or losses, which may not be as apparent to the retail investor if not consistently disclosed in the relevant KID sections. For these types of investment, it is important also to show interim holding periods.

Please also consider our additional remarks on interim performance scenarios and the format of the presentation of costs (Annex V and Appendix 1) below.

### ***Risk and Reward: Presentation of performance scenarios (presentation in graphs)***

#### **Question 15**

*Given the number of tables displayed in the KID and the to a degree mixed consumer testing results on whether presentation of performance scenarios as a table or a graph would be most effective, do you think a presentation of the performance scenarios in the form of a graph should be preferred, or both a table and a graph?*

Keeping in mind our previous comments and our additional comments on performance scenarios below, we favour a graphical representation. However, we are concerned that, as presented, consumers might interpret the plotted lines between the different holding period points as an indication of potential performance over intermediate periods.

Generally, we think a presentation of the performance scenarios in the form of a graph should be preferred to allow easier comparability for retail investors. The consumer testing (p. 47) showed that graphical representation (i.e. “line graphs”) performed equally well as a table with a single holding period. Thus, a graphical presentation allows retail investors to assess different holding periods (especially for time periods before the end of the recommended holding period) while keeping the

performance scenarios as simple, and at the same time being as exhaustive as possible. This would also be more intuitive for the investors and easier to understand, than if solely numbers and percentages were to be disclosed.

Lastly, the presentation of performance scenarios should be future-proof to allow enough flexibility to allow the usage of modern technology, i.e. websites, to better showcase different performance scenarios than is currently possible in paper form.

### Costs: Transaction costs

#### Question 16

*Do you agree with the scope of the assets mentioned in paragraph 25 of Annex VI on transaction costs for which this methodology is prescribed? If not, what alternative scope would you recommend?*

We are strongly against the methodology prescribed by the ESAs to calculate potential transaction costs for a number of reasons.

First and foremost, any methodology must take into consideration that the calculation of Transaction Costs (TC) is simply a future estimate based on three years' of historic data. Its outcome can never be fully accurate, so there should be a cost-benefit trade-off in finding a suitable calculation methodology. Therefore, the proposed TC model is too burdensome to provide future estimates.

Furthermore, the proposed methodology is different from the options consulted upon in the ESAs' Technical Discussion Paper in the summer. The newly proposed model for calculating transaction costs now introduces the concept of an "arrival price" (para. 16). We understand this concept to originate from equity pricing models, but this **methodology is unsuitable to calculate transaction costs**. The below reasons emphasise that a different approach for fixed income and other non-equities is needed.

#### Inclusion of market movements at odds with MiFID II

MiFID II clearly and explicitly excludes market movements from its definition of costs<sup>8</sup>. The re-inclusion through the now proposed methodology is not only legally wrong and but also provides for incorrect assumptions in calculating transaction costs<sup>9</sup>. Market movement is not a cost, but it is part of market risk. What you are calculating is whether or not you have timed your order well. The transaction costs in the proposed model are equal to the exercise price at closing minus the mid-market price at the time the portfolio manager placed the order. The mixing with performance is then so great and the added value is so limited, that its desirability is highly questionable. Also under the proposed methodology it will be possible that a trade could incur negative transaction costs, if the market price at execution is lower than at the time of the order. This is because the price of an instrument may go down after the order is sent. This underlines that the costs would largely depend on the trading model used and is therefore unlikely to promote comparability or predictability of costs for the retail investor.

Furthermore, managers may adapt their transactions by trying to time the market, or by cutting orders into smaller parts, or may aim to time the sending of the order instructions closer to the execution time just to reduce reportable costs. This is not because that will be more cost-effective for the investor

<sup>8</sup> MiFID II Article 24(4)(c): "[...]The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, **which are not caused by the occurrence of underlying market risk**, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return of the investment, and where the client so requests, an itemised breakdown shall be provided. Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment."

<sup>9</sup> It is interesting to note that the ESAs are even contradicting themselves in their approach to transaction costs. On page 80 the ESAs are discussing transaction costs without market movement.

(the larger number of orders suggest it may become more expensive), but because the proposed calculation method makes it appear more cost-effective. (Please see our comments on best execution below).

**Given those comments, we urge the ESAs to redraft these paragraphs and include the principle on the top of page 80 in the draft RTS which defines transaction costs as the “difference between the value of an asset when owned by a PRIIP, and the prices at which the PRIIP transacts in that asset.”**

#### Costs of equity transactions

Fees charged in terms of equity transactions are already captured by letter (j) in paragraph 6 of Annex VI. These comprise broker fees, depositary fees, taxes and potential fees charged by specialised custodians, which already represent the total costs of equity transactions.

#### Costs of non-equity transactions

It is not feasible to calculate transaction costs for fixed-income trades on the basis of the proposed methodology due to the lack of reference data for establishing the relevant arrival prices. Since the arrival price shall reflect the mid-market price at the time the order to transact is initiated, the calculation of the arrival price necessarily implies availability of the relevant data on market prices. In the fixed-income market, however, market prices are not yet transparent enough to assume this required data set<sup>10</sup>. **It is therefore essential to acknowledge that calculations on the basis of such indicative prices are not capable of establishing real transaction costs for fixed-income trades.**

In addition, the approach to determining the relevant arrival price as proposed in para. 16 of Annex VI creates quite significant arbitrage opportunities for calculating transaction costs, thus increasing its susceptibility to errors. Specifically, calculations on the basis of market prices known before the initiation of an order may be used in order to push down transaction costs in case of an anticipated price decrease, possibly based on market developments after the last available quote. In any case, the ESAs should be aware that even indicative quotes for some fixed-income products are often not updated for several hours, or even days, due to the low level of trading activities in certain fixed-income products.

This lack of data is due to the currently inherent structures in the non-equity space. Even though intensive debates are still on-going within the context of MiFID II/MiFIR in order to provide this pre-trade transparency applicable to fixed-income instruments, the outcome of these discussions (in particular the detailed Level-2 measures) is yet uncertain, which means it cannot yet be known whether implementation of MiFID II/MiFIR will even provide, going forward, enough price transparency for PRIIPs manufacturers to calculate the transaction costs as currently envisaged by the ESAs. Currently, it is neither required by EU rules nor considered common practice to record mid-market prices or reference prices in general at a given point of time. The UCITS and AIF rules provide

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<sup>10</sup> A few data vendors such as Bloomberg publish indicative quotes for fixed-income instruments which, however, do not represent real trading quotes since brokers are under no obligation to keep the information up to date.

solely for the duty to record the prices of the portfolio transactions (along with other data points) conducted on behalf of the fund<sup>11</sup>.

Even if MiFID II/MiFIR succeeds in providing the required price transparency in the non-equity space, the required data will not be available at the time of the application of the PRIIP KID Regulation. The ESAs' draft RTS require its calculation on the basis of transactions incurred over the previous three years. This means that, a full set of historical data needed to perform the calculation according to the ESAs' draft RTS will not be possible until three years after the coming-into-force of MiFID II/MiFIR, i.e. earliest in December 2019, but later if implementation of MiFID II/MiFIR is delayed.

This date would even trail the review for the PRIIP KID Regulation by a full calendar year, which suggests that the only sensible solution would be to postpone such a wide-reaching decision (i.e. to introduce such a sophisticated calculation methodology for transaction costs) to coincide with the review of the PRIIP KID Regulation. The feasibility of the proposed calculations should then be appraised in light of the availability of data for the fixed-income markets after the first experiences with the MiFID II transparency regime. Such staggered process would allow the regulators to make evidence-based decisions instead of inventing new standards lacking the compulsory base of market data. In the meantime, the ESAs should revive the hybrid approach to the calculation of transaction costs, which was favoured in the previous round of consultation.

**This means that PRIIPs manufacturers will need to base their spread calculations on the table in para. 25 (currently only envisaged for new PRIIPs) until this required data is available to market participants<sup>12</sup>. Changes to the draft RTS should be made accordingly.**

For further comments on the spread table, also consider our answer to Question 17. Again, this linkage between the PRIIP KID and MiFID II/MiFIR shows the interconnections between these two frameworks and will create further complications once the former comes into force on 31 December 2016.

#### Scope of definition of transaction costs

The PRIIP document rightly mentions anti-dilution fees. These can be deducted from transaction costs. It is however unclear whether all anti-dilution fees have to be reported under entry and exit fees. If this is the case, the ESAs should make clear which types of anti-dilution fees are caught.

#### **Costs: Transaction costs**

##### **Question 17**

*Do you agree with the values of the figures included in this table? If not, which values would you suggest? (please note that this table could as well be included in guidelines, to allow for more flexibility in the revision of the figures)*

<sup>11</sup> Cf. Article 14(2) letter e) of Directive 2010/43/EU (for UCITS), Article 64(2) letter e) of the Implementing Regulation (EU) 231/2013 (for AIFs).

<sup>12</sup> For the avoidance of doubt, this applies to non-equity transactions, while the fees charged for equity transactions are already captured by letter (j) in paragraph 6 of Annex VI.

Please read this answer in conjunction with our reply to Question 16 above.

Generally speaking, it is important to note that the cost table as suggested in para. 25 (page 62f) should be part of Level-3 guidelines rather than Level-2 RTS. The reason for this is that market spreads are a reflection of market volatility and do not remain constant for a period of three years. It is crucial that this table is maintained and updated on a constant basis by the ESAs to provide a relatively accurate description of current market spreads. The currently proposed three-year interval of reviewing the table is therefore not realistic and needs to adapt to the changes in market circumstances. It is necessary that the ESAs regularly and frequently back test the proposed values against actual transaction costs in existing fund portfolios to validate the levels proposed and make updates when necessary. This approach should allow the PRIIP manufacturer to be able to rely on up-to-date cost information when updating the KID on a yearly basis.

We favour using a standardised cost table to calculate implicit transaction cost, which will allow for uniform calculation of transaction costs among all PRIIP manufacturers. This is especially important as the reliance on a standardised spread table will allow smaller PRIIP manufacturers to perform their transaction costs calculation without disproportionate cost, which could put them at a competitive disadvantage.

Also, ESMA should be best equipped to set up and maintain such standardised transaction cost table in view of the transaction data to be collected and processed for MiFID II purposes. In the recent debate on the possible postponement of MiFID II, ESMA itself explained that it is currently running a project called "FIRDS" with the purpose of centralising the collection of reference data which entails direct connections to around 100 trading venues and collection of data on more than 15 million instruments<sup>13</sup>. The FIRDS project is also meant to apply to collecting and consolidating transaction data for the purpose of determining the liquidity status of a financial instrument. We are convinced that this extensive data collection exercise could and should also be utilised in order to establish average transaction cost of financial instruments, including fixed-income products, in the MiFID II environment. However, being aware that the complexity of FIRDS is one of the main reasons for the probable MiFID II delay and will not allow for operational readiness before mid-2017, it is likely that a temporary solution needs to be found. Such a temporary solution could involve, as already mentioned, a table based on reasonable estimations of relevant transaction costs like the one proposed in para. 25.

The importance of this table is further elevated by the fact that (as explained above) market data, in particular for non-equities, will not be available for a number of years. Thus, PRIIP manufacturers will be forced to use this standardised table as no other information is available.

As regards the specific table design, we recommend distinguishing between program and no program trading also in terms of emerging market shares and assuming the explicit costs of listed derivative transaction in absolute numbers in order to reflect the prevailing market practice.

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<sup>13</sup> See Para. 21 of ESMA's note on MiFID/MiFIR implementation: delays in the go-live date of certain MiFID provisions dated 02 October 2015 ([link](#))

Shares emerging markets	Shares emerging markets	<b>Program trading: 4; no program trading: 25;</b>
Listed derivatives	Listed derivatives	<b>0,50 Euro per contract</b>

These adaptations would also help to mark out the relevance of the table for existing products as compared to new PRIIPs: whereas newly launched PRIIPs would need to apply the entire table in order to compute their transaction costs, funds with a relevant trading history would rely only on the assumptions for the implicit cost elements. Explicit costs incurred in existing PRIIPs which comprise in particular broker fees, depositary fees, taxes and potential fees charged by specialised custodians in case of equity transactions would be disclosed on the basis of actual transaction data according to para. 6 (j) of Annex II.

With regards to the asset classes listed, standard industry definitions are needed that correspond to the categories offered to practitioners by data providers such as Bloomberg. UCITS eligible assets were defined by law. It would be beneficial to have also for PRIIPs at least a core set of the most important asset classes.

### **Costs: Monetary amounts**

#### **Question 18**

*Do you agree that the monetary values indicated in the first table are a sum of costs over the respective holding periods? Or should the values reflect annualized amounts? If you prefer annualized amounts, which method for annualisation should be used (e.g. arithmetic average or methods that consider discounting effects)?*

The approach to cost disclosure over the respective holding periods should correspond to the presentation of performance prospects in the risk and reward section. This is of particular importance if, as proposed by the ESAs, the cost disclosure in monetary terms is supplemented by a Reduction in Yield figure to illustrate the effects of costs on performance

In this context, we suggest taking further steps in order to enhance the comprehensibility of the Reduction in Yield concept. Specifically, the term "Reduction in Yield" should be replaced by a description readily understandable for retail investors such as "estimated impact of costs on return". In addition, the introductory part should clearly explain that the impact of costs is calculated on the basis of the moderate scenario displayed in the risk and reward section.

### **Costs: Biometric risk premiums**

#### **Question 19**

*Do you think that estimating the fair value of biometric risk premiums as stated in paragraph 55(b) of Annex VI would raise any technical or practical difficulties?*

Generally speaking, we do not fully understand why the cost of providing life insurance cover should not be fully disclosed. The presented calculation of a "fair value" seems to deduct benefits and to

understate costs. If a guarantee, external to a fund, is provided to a client, then that “benefit” is a cost and should have to be fully disclosed and taken into account in the cost calculation.

As estimating the fair value of biometric risk premiums will raise some technical difficulties, especially linked to underlying asset projection (stochastic modelling, profit-sharing, etc.), we suggest that the ESAs develop Level-3 guidelines on the assumption to be used when calculating the fair value of biometric risk premiums in order to allow a common methodology not only among insurance PRIIPs, but also among other PRIIP types. In any case, we agree with the ESAs that if the insurance undertaking is not able to establish the fair value of a biometric risk premium based on sound estimations of future benefit payments, it should be obliged to include the full biometric risk premium in the cost calculations.

Para. 55(b) allows for profit-sharing mechanisms to be deducted from the costs of an insurance PRIIP. As profit-sharing mechanisms are already part of the performance calculation (see page 52, para. 11(c) in the performance scenarios section), this would allow insurance PRIIPs to add them to the PRIIP's performance and also deduct them from its costs. Profit-sharing mechanisms should be used either to reduce costs or to increase performance, but not both.

### **Costs: Biometric risk premiums**

#### **Question 20**

*Knowing that the cost element of the biometric risk premium is included in the total costs calculation, how do you think the investor might be most efficiently informed about the other part of the biometric risk premium (i.e. the fair value), and/or the size of biometric risk premium overall? Do you consider it useful to include the fair value in a separate line in the first table, potentially below the RIY? Or should information on the fair value be disclosed in another part of the KID (for instance, the “What is this product?” section, where the draft RTS currently disclose biometric risk premiums in total, and/or in the performance section)? What accompanying narrative text do you think is needed, and where should this be placed, including specifically narrative text in the cost section?*

We suggest it would be useful to include the biometric risk premium in the presentation of costs (Annex VII) in the second cost table as “Insurance costs” of a PRIIP. Please see our proposed presentation of costs below.

### **Costs: Amounts to show in table 2 (breakdown of costs)**

#### **Question 21**

*Given evidence as to the difficulties consumers may have using percentage figures, would you prefer an alternative presentation of the second table, solely using monetary values instead? As with the first table, please also explain what difficulties you think might arise from calculating monetary values, and whether this should be on an annualized basis, and if so, how?*

The use of percentage figures would be in line with the existing UCITS KIID and, on the basis of consumer experience, are generally preferred, because actual or monetary figures could be taken

literally by the investor (who might expect fixed costs and not understand if the indicated amount is different in practice). In particular, recurring costs expressed in monetary values could be misleading for the investor. We are not aware of any concerns raised by investors into UCITS as a result of using percentage figures in the KIID.

Nevertheless, we believe that these percentages should not be in the form of RIY figures based on the RHP. As the first table is showing the effect of charges, it would be most useful if the second table showed the actual cost structure, thereby enabling a proper understanding, and even replication of the cost structure in other scenarios. It is likely to be misleading to show a 5% entry cost as 1% in the hope that the investor realises that the table relates to a recommended holding period of 5 years and the 5% has been amortised. These actual percentages are also what will be used by online calculators and required by MiFID II.

Please consider our revised breakdown of costs template below for further information.

#### **Costs: Alternative presentation of cost breakdown**

##### **Question 22**

*Given the number of tables shown in the KID, do you think a more graphic presentation of the breakout table should be preferred?*

Even though the KID already contains a number of tables, the vital information on costs portrayed to the retail investors necessitates a summary table as well as a detailed breakout table. The table has the decisive advantage of accommodating cost impacts for different holding periods which is difficult to accomplish in the graphic.

A more graphic presentation may oversimplify different types of costs and may make it harder to understand the differences between particular types of PRIIPs. It may also not provide the cost breakdown as required by MiFID II and should therefore be avoided.

#### **Costs: Alternative presentation of cost breakdown**

##### **Question 23**

*The example presented above includes a possible way of showing the variability of performance fees, by showing the level for all three performance scenarios in the KID, highlighting the 'moderate' scenario, which would be used for the calculation of the total costs. Do you believe that this additional information should be included in the KID?*

The example proposed in the paper above Question 23 provides detailed information on performance fees but does not showcase the variability of other cost elements. Investors could be induced to assume that, since only the performance fee figures are presented as variable in different market conditions, other costs will remain stable in any case. This impression should be avoided given that the

recurring cost figure is also meant to comprise transaction costs which may vary considerably depending on the market situation and the portfolio composition at a specific point of time.

We are, thus, in favour of the summary table as well as a detailed breakout table as explained above.

### **Costs: Alternative presentation of cost breakdown**

#### **Question 24**

*To reduce the volume of information, should the first and the second table of Annex VII be combined in one table? Should this be supplemented with a breakdown of costs as suggested in the graphic above?*

We are not in favour of combining both tables, as the second table rather provides clarity on the information included in the first table. Please consider our suggested revised summary and detailed breakout tables below.

### **Costs: Reduction in Yield (RIY)**

#### **Question 25**

*In relation to paragraph 68 a) of Annex VI: Shall the RTS specify that for structured products calculations for the cost free scenario have always to be based on an adjustment of the payments by the investor?*

Yes, the RTS could specify that for structured products, calculations for the cost free scenario have always to be based on an adjustment of the payments by the investor, as investors in structured products often have no possibility to make additional investments after the initial subscription.

### **Costs: Presentation format (Annex VI "Methodology for the calculation of costs")**

#### **Question 26**

*Regarding the first table of the cost section presented in Annex VII, would you favour a detailed presentation of the different types of costs, as suggested in the Annex, including a split between one-off, recurring and incidental costs? Alternatively, would you favour a shorter presentation of costs showing only the total costs and the RIY?*

#### **Question 27**

*Regarding the second table of the cost section presented in Annex VII, would you favour a presentation of the different types of costs showing RIY figures, as suggested in the Annex, or would you favour a presentation of costs under which each type of costs line would be expressed differently, and not as a RIY figure -expressed as a percentage of the initial invested amount, NAV, etc.?*

As explained above, we are in favour of showcasing both a summary table and a more detailed breakout table as suggested by the ESAs.

The currently proposed summary table on page 73 is nevertheless a hybrid between a summary and breakout table. We recommend a simpler summary table followed by a more detailed breakout.

By way of introduction, please note the following:

- As the first table is showing the effect of charges, it would be most useful if the second table showed the actual cost structure, thereby enabling a proper understanding, and even replication of the cost structure in other scenarios. It is likely to be misleading to show a 5% entry cost as 1% in the hope that the investor realises that the table relates to a recommended holding period of 5 years and the 5% has been amortised. These actual percentages are also what will be required by MiFID II and will be used by online calculators.
- While in favour of the reduction-in-yield methodology, we question whether the concept "RIY" is understood by the average retail investor. We therefore propose (see comments on Annex VII's presentation of costs) to describe RIY in plain language such as "equivalent annual percentage rate".
- The ESAs' proposal misses a link to the performance scenario, i.e. indicating that the costs are based on the moderate performance scenario.
- Each of the detailed cost items should be shown only if relevant. The below example showcasing a fund's costs should thus delete the lines on "exit costs", "insurance costs", "carried interest" and "exit penalties" in the final version.

## What are the costs?

This section tells you the effect that costs might have on what you get back from your investment and explains the different types of costs. The amounts shown are the costs of this product. Your adviser or the person selling you this product will tell you about any additional costs of distribution not included in these amounts.

<b>Estimate of costs over time</b>	<b>Over 5 years</b>		
<b>If you invest €1,000</b>	<b>Over a year</b>	<b>Over 3 years</b>	<b>(recommended)</b>
Total impact of costs over each time period	€ 53	€ 85	<b>€ 125</b>
Equivalent annual percentage rate (N.B. "RIY")	5,3%	2,6%	<b>2,2%</b>

The table above shows you the estimated impact of costs on what you might get back from your investment. To see what you might get back after these costs you should read the performance scenarios section of this document.

The table above is based on the moderate performance scenario and assumes you invest €1,000 and leave it invested for the time periods shown. The costs used are estimated based on data from the past and therefore are likely to be different in the future.

### The costs explained

#### One-off costs taken before or after your money is invested

<b>Entry costs</b>	<b>3,00%</b>	This is the maximum that might be taken out of your money before it is invested. In some cases you might pay less.
<b>Exit costs</b>		This is the maximum that might be taken out of your money before the proceeds of your investment are paid to you. In some cases you might pay less.

#### Costs taken from the product over a year

<b>Recurring costs</b>	<b>0,80%</b>	This is taken from your investment each year to cover the costs of managing and operating the product. The figure shown is based on actual costs for the year ending xx/xx/xx.
<b>Insurance costs</b>		This is taken from your investment each year to cover the cost of your insurance cover. The figure shown is based on actual costs for the year ending xx/xx/xx.
<b>Transaction costs</b>	<b>0,50%</b>	This is incurred each time the fund's underlying investments are bought and sold. The figure shown is the yearly average for the last three years. These costs vary depending on the frequency of buying and selling and the nature of the investments involved.

#### Costs taken from the product under certain specific conditions

<b>Performance fees</b>	<b>1,00%</b>	We charge a performance fee of 20% of any outperformance only when the product outperforms its benchmark, the [name of benchmark]. The figure shown is the yearly average for the last five years. The performance fee varies depending on the performance of both the product and the benchmark and may not arise at all.
<b>Carried interest</b>		Our carried interest in the product is 20% of the profits generated each year. The figure shown is the yearly average for the last five years.
<b>Exit penalty/Exit cost</b>		An exit penalty will apply if you leave early. The figure shown is the maximum which applies if you leave in the first year. The exit penalty does

		not apply if you hold the product for at least five years. (N.B. The intention is to cover any penalties/costs that are not included in the one-off "exit costs")
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### Impact assessment

#### Question 28

*Do you have any comments on the problem definition provided in the Impact Assessment?*

*Are the policy issues that have been highlighted, in your view, the correct ones? If not, what issues would you highlight?*

*Do you have any views on the identified benefits and costs associated with each policy option?*

*Is there data or evidence on the highlighted impacts that you believe needs to be taken into account?*

*Do you have any views on the possible impacts for providers of underlying investments for multi-option products, and in particular indirect impacts for manufacturers of underlying investments used by these products, including where these manufacturers benefit from the arrangements foreseen until the end of 2019 under Article 32 of the PRIIPs Regulation?*

*Are there significant impacts you are aware of that have not been addressed in the Impact Assessment?*

*Please provide data on their scale and extent as far as possible.*

From discussions with practitioners we are of the view that clarification in many respects is still needed. According to Art. 6 Para. 7 of the draft RTS (on page 25 of the Consultation Paper), the ESAs will also legally be required to establish further guidelines. As a result, it will be very difficult, and probably impossible, for many product manufacturers to make available a PRIIP KIDs as from January 2017. A delay in implementation is therefore essential.

We also strongly oppose the ESAs' view that would require multi-option product (MOPs) to provide information on underlying investment options through a PRIIP KID. This clearly oversteps the Level-1 Regulation which simply requires "generic description" of these underlying investment options which can undoubtedly be satisfied by providing a UCITS KIID to investors (for those funds being already required produce a UCITS KIID).

The exemption granted by Article 32 of the PRIIP KID Regulation for UCITS and the many other nationally regulated retail funds that produce the UCITS KIID should not be undermined by conflicting rules applicable to other PRIIP providers. The unsatisfactory situation presented on page 123 of the Consultation Paper (first bullet point under the section *MOPs Costs*) should be taken into account with high priority by the legislator before the new rules are finalised. As drafted, the MOP rules would require a very large number of investment funds to produce both a UCITS KIID and information for a PRIIP KID, at least until 31 December 2019. This would also undermine the review by the Commission pursuant to Article 33 of the PRIIP KID Regulation. Moreover, and very importantly, it would result in confusing information for investors, with the core features of risk, performance and costs presented differently in the two documents.

We deem it questionable whether such outcome was envisaged by the EU legislators or even is covered by the Level 1 text. Article 6(3) of the PRIIP KID Regulation stipulates that in the case of MOPs "the key

information document shall provide at least a generic description of the underlying investment options and state where and how more detailed pre-contractual information documentation relating to the investment products backing the underlying investment options can be found." In our view, this wording does not imply provision of a PRIIP KID for each of the underlying investment option. On the contrary, when combined with Article 32 it should be read as allowing the provision of the UCITS KIID as pre-contractual information on any UCITS or AIF benefitting from the exemption under Article 32.

**Against this background, we urge the ESAs to reconsider their having regard to the wording of Article 6(3) of the PRIIP KID Regulation and the EU legislator's deliberate choice to spare investment funds providing a UCITS-like KIID from the duty to implement new information standards until the end of 2019.**

Overall, however, we expect that the impact of the Level-2 measures on the fund industry in terms of both financial resources and operational efforts will then be much higher than expected by the EU legislator. Many fund management companies will be effectively compelled to set up internal projects in order to provide their business partners from the insurance sector with PRIIPs-compliant SRI, performance scenarios and cost figures. Such elements should in principle be delivered well ahead of the entry into force of the PRIIP KID Regulation in order to enable, for instance, insurance companies to produce PRIIPs KIDs on unit-linked insurance products on time. Since the specific standards for MOPs were not discernible before publication of the draft RTS in November 2015 (and are still unclear today), most fund providers have not yet assigned specific budgets or set up business projects for PRIIP KID implementation. If they had to be planned and implemented as a matter of urgency, such projects would probably entail disproportionately high costs. **In any case, it is utterly inappropriate to assume that above all things fund providers must be ready for the PRIIP KID regime going live well ahead of its formal implementation date even though they manage the only sort of PRIIPs for which a temporary exemption from scope applies.**

Last but not least, we require further clarification with regards to Recital 20<sup>14</sup> that a periodic review of the KID is required only if the PRIIP manufacturer is actively supporting the distribution of a PRIIP on the secondary market. We are aware of instances where funds have been sold on the secondary market without the knowledge of the PRIIP manufacturer. In such cases it should be the obligation of the distributor (and not the manufacturer) to ensure that an up-to-date KID exists when an investor intends to purchase a PRIIP on the secondary market. In other words, it must be ensured that there is no obligation for the PRIIP manufacturer actively to scrutinise the secondary market simply to ensure that its products are not sold without an up-to-date KID even though this was not intended by the manufacturer.

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<sup>14</sup> Recital 20 states that "[...] *The trading of a PRIIP on a secondary market however would not exempt the PRIIP manufacturer from the obligation to continue to review and revise the key information document for that PRIIP.*"

## [Additional comments relating to the draft RTS not covered in the Questions](#)

In addition to our answers to the ESAs' questions, EFAMA would also like to provide the ESAs with the following detailed comments on the draft RTS and its Annexes.

### [Article 3: Identity section](#)

#### [Article 3\(f\)](#)

"The date of the production and of any *subsequent* revision of the key information document" is required sub-paragraph (f) to be stated in the KID. The wording "any *subsequent* revision" could be misunderstood to refer to the dates of all the subsequent revisions, adding no useful information to the investor. **We therefore propose that the article instead refers to "the date of the production and of the latest revision of the key information document".**

### [Article 4: 'What is this product?' section](#)

#### [Article 4\(3\)](#)

According to letter b. the description of the PRIIPs "underlying investments or reference values" has to be very detailed. A generic description is possible only where the "number of specific investments is large". In the case of UCITS the criterion of the number of investments is inadequate because the investments of UCITS are made on the basis of the principle of risk diversification. Also a considerable number of retail AIF managed on the basis of UCITS risk diversification rules or comparable rules for the specific market segment. In addition, actively managed UCITS and AIFs are not built upon a stable portfolio, but comprise assets that are bought and sold in accordance with the agreed investment strategy.

Therefore, more flexibility is needed under the general description of letter (b). **Thus letter (b) should be amended as follows:** "(b) on underlying investment assets or reference values may only refer to market segments or instrument types where the number of specific investments **are numerous or can be continuously purchased and sold according to the investment policy and strategy of the PRIIP**".

#### [Article 4\(4\)](#)

Article 4(4) proposes to include "the target market identified by the PRIIP manufacturer's product oversight and governance processes". The referenced Article 8(3)(c) of the PRIIP KID Regulation merely requires "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". The addition of "product oversight and governance processes" does not exist in the Level-1 Regulation and thus would

require non-MiFID firms, such as UCITS Management Companies and AIFMs, to apply the MiFID II product governance and oversight rules for product manufacturers, which was not intended in the Level-1 Regulation. **Therefore the above mentioned sentence should be amended as follows: “the target market identified by the PRIIP manufacturer.”**

Moreover, the ESAs' proposal goes even further by stating that these product oversight and governance processes need to take into account “*the financial interests, knowledge, objectives and characteristics of the types of retail investors for whom the PRIIP has been designed...*”. This goes beyond the product oversight and governance processes<sup>15</sup> requirement of the to-be-released draft MiFID II Delegated Directive, which are not expected to require the product manufacturer to specify a target market according to *financial interests, knowledge and objectives*. The PRIIP KID Regulation is meant to provide product disclosure and should not introduce new governance requirements through the Level-2 measures. **These aforementioned requirements should therefore be replaced with a reference to Art. 16 para. 3 of MiFID II and Art. 25 of draft IDD.**

#### Article 6: Performance scenarios

Taking into consideration our reply to Q14, we agree with Article 6(2) that “performance scenarios shall be defined for the recommended holding period and for certain holding periods in between, when appropriate.” In order to receive further necessary clarity, we suggest that the ESAs establish guidelines (as suggested in para. 7) that further define (i) for which PRIIPs it is appropriate to provide performance scenarios and (ii) when it is appropriate to do performance scenarios for periods before the end of the recommended holding period.

With regards to the three suggested scenarios, we are generally supportive of the ESAs' approach to defining unfavourable, moderate and favourable scenarios as presented in Annex IV and we also support the ESAs' intentions to provide further technical guidance in Level-3 guidelines for non-linear products such as structured products and life-cycle funds.

Having said this, it is important that the ESAs deliver these guidelines without undue delay to provide PRIIP manufacturers with the necessary specificities to properly and appropriately design and calibrate these scenarios. Given that the drafting of and consultation on these guidelines will understandably take some further time, it is very likely that the publication of these guidelines will happen well after the publication of the PRIIP KID Implementing Regulation. This underlines the need for a delay in the PRIIP KID Regulation coming into force, to allow national competent authorities and industry enough time to implement the rules.

In addition, we have concerns regarding interpretations relating to Article 9 in relation to performance scenarios. The fund industry currently uses past performance as the indicator for investors as to how the fund is run and provides them with valuable information. The UCITS KIID currently requires performance to be shown by way of annualised past performance. We would be very concerned if the

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<sup>15</sup> MiFID II Commission Delegated Directive; Article 9(9)-(12)

requirement to produce performance scenarios in the PRIIPs KID would ultimately mean that on conversion to the PRIIPs KID, the view was taken that funds could no show past performance – it might, for example, be interpreted as ‘diminishing the significance of the key information document’. **We would therefore be grateful for confirmation by the ESAs that producing documentation which included past performance would still be acceptable following the introduction of the PRIIPs KID for funds.**

For more technical observations, please regard our comments on the Annex IV below.

#### [Article 7: ‘What happens if \[the name of the PRIIP manufacturer\] is unable to pay out?’ section](#)

An additional paragraph providing information on the structure of funds is necessary to complement para. 2 on investor compensation and guarantee schemes. This paragraph should explain that a fund’s assets are held separately from the management company and safeguarded by a depositary. A pay-out of the fund’s assets is thus not affected by a management company’s financial position or potential default.

Please also regard our answer to Question 5.

#### [Article 10: ‘How can I complain?’ section](#)

While we are generally in agreement with the drafting of Article 10. However, it currently requires the PRIIP manufacturer to provide information on “the person advising on, or selling, the PRIIP on the relevant website”. This assumes a direct connection between the PRIIP manufacturer and distributor, which is not always the case. In particular, for funds information about who will be advising on or selling the PRIIP is rarely known by the manufacturer. **This information should thus be deleted.**

#### [Article 11](#)

“Without prejudice to ad hoc reviews” should not be part of the information on the updating period. It could just be omitted because this information is not relevant for the investor. It conflicts with the plain language requirement and the restriction to three pages.

#### [Articles 12-15: Specific provisions on the key information document \(i.e. Multi-investment option PRIIPs\)](#)

We are thankful for the clarification that the PRIIP manufacturer is responsible for the provision of the KID, but nevertheless think that the ESAs’ current drafting oversteps the Level-1 text<sup>16</sup> which merely

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<sup>16</sup> PRIIPs Regulation Art. 6(3)

necessitates Multi-investment option PRIIPs (MOPs) to provide “at least **a generic description** of the underlying investment options and **state where and how more detailed pre-contractual information documentation** relating to the investment products backing the underlying investment options **can be found.**” This is due to the fact that Articles 12-15 (in particular Articles 12(1)(a) & (b) and Article 15(2)) as currently consulted on by the ESAs would de-facto require asset managers to provide “PRIIP KID-like” data to other providers, such as insurance companies. This unwarranted outcome is even acknowledged by the ESAs in the consultation paper<sup>17</sup>.

The Level-1 text, for this very reason, therefore specifically requires only “pre-contractual information documentation” such as the UCITS KIID. Until the review of the UCITS exemption in 2019, the ESAs should allow such to be as sufficient, since it would otherwise undermine the UCITS KIID’s pre-contractual nature before the legislators’ decision on the matter. Only in 2019, if the co-legislators decide not to prolong the UCITS KIID going forward and instead require the PRIIP KID for all types of PRIIPs, should the full PRIIP information then be required for funds currently providing a UCITS KIID. But, in any case, the KID of the MOP wrapper (a KID itself) would still provide at least the “generic description” mentioned in Article 6 paragraph 3 of the Level-1 Regulation.

Furthermore, the ESAs should also take into consideration what type of pre-contractual information will be presented to retail investors in the near to medium future. Since UCITS are legally required to provide a KIID until at least 2019, investors will always receive a KIID when investing directly into a UCITS. If MOPs were required to provide a PRIIP KID for the underlying investment options, then retail investors would receive different pre-disclosure information based on whether they are investing into a UCITS directly (i.e. KIID) or through a unit-linked insurance (i.e. KID). This is unsatisfactory, and will create unnecessary confusion for consumers.

Therefore, Articles 12-15 need to be redrafted in order to comply with the Level-1 framework. See also our response to Question 11 regarding the risk indicator shown by the insurance MOP wrapper.

#### [Article 16-20: Review, revision and republication of the key information document](#)

##### *Recital 19: Use of mailing lists*

**Recital 19 needs to be either deleted or clarified further**, as it states that “[t]ools, such as mailing lists or email alerts, might be implemented to inform existing retail investors when key investor documents are revised”, which creates untrue statements. First, the KID is a pre-contractual document and is thus not designed to update current investors. Secondly, the current wording blurs the roles and responsibilities between manufacturers and distributors. It is the sole responsibility of the

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<sup>17</sup> Page 123 on MOPs Costs: “[...] In so far as the insurance undertaking requests that the UCITS to already prepare KID compliant information for the insurance undertaking – though this is not directly required under the PRIIP Regulation -- this would have the practical impact of undermining the temporary exemption in the Regulation and requiring UCITS to produce simultaneously a KII and KID-compliant information.”

manufacturer to review, revise and republish the KID on his website. If possible, it can inform its known distribution network of the revised KID. It is not possible for the manufacturers to inform the investors, as most manufacturers are not aware who the end investors are and often do not have direct contact with them.

*Recital 20: Periodic review of a PRIIP on a secondary market*

First, please consider our comments to Q28 above.

Second, in order to create more clarity among practitioners, **we suggest Article 16(1) is amended as follows: “The PRIIP manufacturer shall review the information contained in the key information document at the latest by”.**

Article 17: Ad hoc review of the key information document

**Article 17 is missing an all-important “materiality” reference.** This exists in the UCITS KIID requirements and ensures that only material changes trigger an ad hoc review of the KIID. This is important, as it ensures that minor and inconsequential changes do not require the PRIIP manufacturer to perform an ad hoc review.

The triggers should be substantial, meaning that the change should have a significant impact on the investment risk, return scenarios and/or cost, taking into account how relevant the change is from an investor perspective. Subjective criteria's might be appropriate to some extent (e.g. it should be clarified when changes in the technical risk indicator trigger a requirement to update the KID).

Article 20: Conditions on good time<sup>18</sup>

The conditions for delivery in good time should make reference to the relevant passages in MiFID II, IDD and the PRIIP KID to ensure consistent application of the distribution requirements for all types of PRIIPs. **We therefore suggest to align Article 20 with Article 80(1) of the UCITS Directive 2009/65/EC).**

ANNEX I: OVERALL KID TEMPLATE

We have no particular comments on the template of the KID, but wonder how prescriptive its design is and how close a PRIIP KID has to resemble Annex I (not relating to its content, but rather to its formatting, font, colour, size, etc.)?

Furthermore, it is not totally clear how the mock-up contained in Appendix 1 of Annex III will work with the template in Annex I. For example, the template refers to Summary Risk Indicator and narrative text pursuant to Article 8(3)(d) and Appendix 1 of Annex III provides various ‘elements’ a – o which may or may not need to be included. The chart provided on page 49 of the 1-7 scale, includes words in

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<sup>18</sup> For the avoidance of doubt and given that there are two Articles 20 in the CP, we are referring to page 31.

brackets underneath the scale alongside a warning triangle. But that wording does not equate to the wording provided in the various elements a - o. So, does this mean that the chart is meeting PRIIP KID Regulation Article 8 3.(d)(i) ('a summary risk indicator supplemented by a narrative explanation of that indicator, its main limitations, etc.) and the elements a - o meet the requirements of Article 8 3 (d)(ii)?

## ANNEX II: METHODOLOGY OF RISK CALCULATION

### Part 1: Methodology for the market risk assessment

First and foremost, we unfortunately must note that the current drafting of the "methodology for the market risk assessment" is of poor quality, to the extent that certain passages are illegible and therefore unusable. We urge that this section be redrafted for easier understanding.

#### Para. 1-19: PRIIP categories

Please first consider our important comments to Q3 and Q8 regarding the creation of a separate MRM class for PRIIPs where the maximum loss may exceed the money invested.

#### *PRIIP categories from a fund's perspective*

Taking the above comments into consideration, we are very unclear into which PRIIP category UCITS and AIFs fall, which is of utmost importance, as the MRM calculation is dependent on the PRIIPs categorisation. It is our general understanding that funds may fall into the following categories:

- *Category I(a)*

E.g. a fund with maturity of up to five years with an unconditional protection of capital by a third party? It should also be clarified that the unconditional protection of capital refers to all the capital and not only to a percentage of it (e.g. 95%).

- *Category II: Linear pay-off profile UCITS and AIFs*

Category II appears to include linear pay-off profile UCITS and AIFs and thus the bulk of fund products. If this assumption is correct, we ask the ESAs to redraft in particular the last two paragraphs of para. 10<sup>19</sup> that seem to be applied together. First, the second last paragraph on page 35 states that

*"where these PRIIPs have, either directly or on a synthetic basis, a delta one or a leveraged exposure on underlying asset(s) that pays a constant multiple of a market price or index"*

which creates questions about what is meant to be captured by "a constant multiple of a market price or index" and whether the reference to leverage is also linked to any definition of leverage within the AIFM Directive. Second, the last paragraph on page 35f states that

*"where at least 2 years of historical daily prices or 4 years of historical weekly prices are available, or, in the case where such minimum data are not available, where a natural*

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<sup>19</sup> Please note that the UCITS Directive is also wrongly referenced, as it currently refers to MiFID II.

*benchmark or proxy exists (e.g. recently created ETF on a liquid market index), such that the data of this benchmark or proxy shall be used, on a complementary basis, in the calculation of the market risk."*

We do not understand the intended meaning of a "natural" benchmark and wonder whether the ESAs meant "pre-existing" benchmark? In any case, it is important to note that there are no linkages with the currently agreed Benchmark Regulation, which creates further requirements around the use of a benchmark.

- *Category III: Non-linear pay-off profile UCITS and AIFs (i.e. structured UCITS and AIFs)*

We ask the ESAs to take the above remarks into consideration and amend the RTS accordingly.

**The correct definition of Category II funds is paramount, as Category III funds are simply defined as "any AIFs and UCITS not falling under Category II".** An imprecise Category II definition could result in some types of funds to be considered as structured funds for its MRM calculation.

Furthermore as Category III funds are simply defined as "any AIFs and UCITS not falling under Category II", it seems that also funds with an insufficient amount of data would fall under Category III. These types of funds should be excluded from Category III.

This is particularly relevant for two points of para. 17<sup>20</sup>. As explained further below (Para. 20-29), we believe that use of daily prices will create unnecessary noise for the calculations. Instead, at most weekly or monthly prices should be used. Secondly, the reference to 500 historical data prices contradicts the later mentioning of 5 years' data.

- *Category V: Fund with insufficient amount of data or holding illiquid assets*

In our understanding, to assess the MRM for funds with insufficient history and for which is not possible to use a benchmark or proxy a qualitative approach should be used. The ESAs suggest a table with different risk categories on the basis of the "type of the funds".

We have some concerns about this proposal because the MRM class for a new absolute return or total return fund with a dynamic allocation seems always to be 5 at the minimum and this would not always be correct. An incorrect risk representation could also incur for other types of funds which have a dynamic asset allocation between the same "type of funds". We also ask the ESAs to clarify para. 13(a)(ii) with regard to insufficient data. Indeed, the added value of this statement is unclear, as there are other paragraphs already dealing with rules on insufficient data: Category II, par. 10 last sentences ((2 years historical daily prices or 4 years of historical weekly prices/proxy are available) and Category V, par. 17.

#### [Para. 20-52: Calculation methodology of MRM](#)

We regrettably also consider the drafting of the MRM methodologies of overall low quality and in some places technically wrong, as was confirmed by the ESAs through the publication of an errata. The initial feedback we received by experts was that the current drafting is unnecessarily complex and should

<sup>20</sup> "The MRM of Structured PRIIPs shall be assessed based on the methodology detailed in Paragraphs 30 to 48, provided that at least 500 historical daily prices of such Structured PRIIPs' underlyings are available in relation to the last 5 years. Where such data is not available, the Structured PRIIP shall be assigned to Category V."

thus be simplified. Notwithstanding our below comments, it is of utmost importance that the language and formulas used (i.e. convention of terminology, symbols, and formulas) in this section is understood by quantitative analysts that are ultimately responsible for the calculation of the MRM. Going into more detail, we have the following remarks.

#### Para. 20-29: "Cornish Fisher" VaR for Category II PRIIPs

The ESAs suggest to use daily prices for the VaR calculation. Daily prices produce much "noise", which will distort the VaR calculations. Instead, weekly prices or monthly should be used, which will still allow for enough sample data to be collected. The use of weekly prices or monthly prices, where possible, in line with the UCITS SRI methodologies also overcomes operational problems for funds that do not have a daily NAV.

Also, the VaR calculation is based on the recommended holding period (RHP) in years (para. 28). Since this assumed RHP may be different from one manufacturer to the next, this may result in different MRM for the same underlying of a PRIIP due to differently assumed RHPs.

#### Part 2: Methodology for the credit risk assessment

##### *No credit risk assessment for AIFs and UCITS*

We strongly support para. 54 (p. 40), which states that credit risk shall not be assessed for AIFs and UCITS. Nonetheless, a statement is missing that these UCITS/AIFs are therefore automatically categorised as CR1. Additionally in order properly to inform investors, the KID should include a short statement that these UCITS/AIFs do not carry Credit Risk (CR).

Nevertheless, while certain UCITS and AIFs are exempted, the explanatory text for para. 55 lit(b), page 76, makes direct references to AIFs, which requires further clarification from the ESAs. Instead of "AIFs", we believe it should correctly refer to "structured notes".

##### *Credit risk classes*

First, after the EU co-legislators' efforts to reduce the dependency on Credit Rating Agencies (CRAs), we find it surprising that the credit risk measured is to be based solely on external credit ratings. We suggest that this section should levy more on other pieces of legislation and legislative frameworks rather than "hard wiring" certain CRAs into the PRIIP KID Level-2 RTS.

### Credit quality steps

Please note that that paragraph 62 erroneously refers to “paragraph 57(c)” instead of “paragraph 57(iii)”.

### Part 3: Aggregation of market and credit risk into the summary risk indicator

Again, as mentioned above and for the avoidance of doubt by retail investors, it should be clarified that UCITS and AIFs within the meaning of para. 54 should fall within the CR1 credit risk-class.

Generally speaking, it seems that when aggregating market and credit risk into the summary risk indicator, credit risk is underrepresented when compared to market risk. We believe that MRM and CRM should carry equal weightings.

### Part 5: Liquidity risk

While we have no major remarks regarding para. 74-76, we would ask for further clarity around the language that is being used in the relevant paragraphs.

For example para. 76(d) talks about “significant” early exit penalties. Does this have any significance for funds with predefined maturity, and when must early exit penalties be considered “significant”? It should also be ensured that that such penalties cannot simply be classified as “costs” in order to escape this assessment and its subsequent disclosure as an additional risk. Also, please provide further clarification as what is considered to be a “long” disinvestment notice.

### Part 6: Currency Risk Assessment

Please see our answer to Question 12.

## ANNEX III: METHODOLOGY FOR THE PRESENTATION OF SUMMARY RISK INDICATOR

### Appendix 1: Format of Presentation of the Summary Risk Indicator

With regards to the presentation of the currency risk, please consider our above comments and our answer to Question 12.

## ANNEX IV: TECHNICAL RULES OF PERFORMANCE SCENARIOS

Please also consider our answer to Question 14 as well as comments to Article 6(7) above.

## ANNEX V: PRESENTATION OF PERFORMANCE SCENARIOS

Please also consider our answer to Question 14 as well as comments to Article 6(7) above.

Generally speaking, guidelines are required to avoid that PRIIPs manufacturer will potentially spawn a multitude of various approaches and a risk/return that this will be used as a competition or marketing element.

### Appendix 1: Presentation of Performance Scenarios

With regards to the proposed presentation in Appendix 1, we wonder why there are two almost identical tables presented on page 55? Should one consider that the first table is used for one-off investments, whereas the second table is meant for investment connected to an investment plan (as it includes “accumulated invested amount”)? We seek clarification.

## ANNEX VI: METHODOLOGY FOR CALCULATION OF COSTS

### Part 1: List of costs of the different types of PRIIPs

#### Section I: List of Costs of investments funds (AIFs and UCITS)

We understand that this list of costs of investment funds is based on the currently applicable CESR guidelines. In particular, it seems that the underlying motive for this new cost list was to define as many costs as possible with different terminologies, instead of describing the underlying reason(s) for these types of costs to occur in the first place. This creates unnecessary ambiguities that can be avoided by using the approach used in the UCITS KIID guidelines. In particular, since it already covers all costs described in the “one-off” and “recurring” section.

#### One-off costs

Keeping our above comments in mind, we ask for further clarification of what is meant by a cost “borne by the fund” (para. 2). Our understanding would be that such a cost is a recurring cost rather than a one-off cost. Additionally, we do not understand the term “loading costs” (para. 3(b)) and wonder whether this is the same as subscription costs?

#### Recurring costs

We have several observations on the recurring cost section.

First, para. 6(b) sub point (v) contains both “securities lending” and “property management”, which are two distinctively different outsourced services and should thus be separated in their own sub points. Furthermore, “capital expenditure” should not be included in the costs together with other operating expenses. “Capital expenditure” is a capital investment made directly on the assets with the effect of increasing the value of an asset (i.e. repairing the roof of a building) and thus is not an outsourced service. Its reference should be deleted.

With regard to para. 6(i), we agree on the wording, but we strongly disagree with the explanatory text on page 79. Option premiums are not costs. Generally speaking, the total price paid to invest into an asset (whether it be a stock, a bond or an option) is not a cost. Only a little part of the total price is cost (like brokerage fee). Furthermore, this explanatory text contradicts §18(c) on page 61.

As regards costs of underlying investments, the wording in paragraph 6(l) and (m) is very ambiguous and should be rectified by deleting the first subparagraph and starting right away with the respective subparagraph (i). In our view, the correct provision should read as follows (taking the example of 6(l)):

(l) the costs of acquiring or disposing of units in UCITS or AIFs shall be taken into account in accordance with the following steps:

(i) Where a fund invests its assets in UCITS or AIFs, its summary cost indicator and recurring ratio shall take account of the charges incurred in the underlying UCITS/AIFs. The following shall be included in the calculation:

(ii) if the underlying is a UCITS its most recently available recurring and entry/exit charges figure shall be used; this may be the figure published by the UCITS or its operator or management company, or a figure calculated by a reliable third-party source if more up-to-date than the published figure; [...]

Lastly, we believe that para. 6(q) contains a drafting error: it should be referencing either “section II” not “paragraph 2”, or para. 37 (page 65f) which discusses “implicit costs of PRIIPs other than investments funds”. It seems to refer to implicit costs of derivatives entered into by funds. Those derivatives often do not qualify as PRIIPs, so their implicit costs will not be disclosed by counterparties. Para. 37 and following could not be applied, because asset managers are not able to compute the “fair value” with the same accuracy as investment banks. If the implicit costs incurred by funds have to be disclosed, then regulation should oblige counterparties (investment banks) to disclose them to asset managers.

#### Transaction costs

Please consider our answers to Questions 16 and 17.

Furthermore, the reference to customised derivatives is not understandable and in contradiction with para. 6(q) on page 59.

#### Performance Fees

For more detailed comments on the presentation of the Performance Fees, please consider our comments above on Annex V.

### [Section II: List of costs of PRIIPs other than investment funds – including structured products, derivatives and contracts for difference \(CFDs\)](#)

With regards to para. 32 on page 65 we suggest adding the following item: “direct or indirect costs associated to the structure of the product in relation to prudential requirements (own funds, liquidity, etc.)”. Also, we suggest adding the following to para. 26: “any recurring cost similar to those listed in paragraph 32”.

### [Section III: List of Costs of Insurance-based investment products](#)

Please consider our response to Question 19 above.

In addition, all costs incurred in a fund that can be incurred by an insurance company in the manufacturing/managing of a PRIIP should be included. Alas, the same rules should be applied.

**Part 2: Summary indicators**

While having no technical remarks on the actual Reduction-In-Yield methodology, we question whether the concept "RIY" is understood by the average retail investor. We therefore propose (see comments on Annex VII's presentation of costs) to circumscribe RIY with something more understandable such as "equivalent annual percentage rate".

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Brussels, 25 January 2016

[16-4007]