German Banking Industry Committee

Die Deutsche Kreditwirtschaft

Comments

GBIC comments to the Joint Consultation Paper PRIIPs Key Information Documents – Draft regulatory technical standards –(JC 2015 073)

Register of Interest Representatives
Identification number in the register: 52646912360-95

Contact: Klemens Bautsch
Telephone: +49 30 20225- 5254
Telefax: +49 30 20225- 5665
E-Mail: klemens.bautsch@dsgv.de]

Contact: Sebastian Brinschwitz
Telephone: +49 30 20225- 5376
Telefax: +49 30 20225- 5665
E-Mail: sebastian.brinschwitz@dsgv.de]

Berlin, 8. Februar 2016

The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent approximately 1,700 banks.

Coordinator:
German Savings Banks Association
Charlottenstrasse 47 | 10117 Berlin | Germany
Telephone: +49 30 20225-0
Telefax: +49 30 20225-250
www.die-deutsche-kreditwirtschaft.de

Comments to the Joint Consultation Paper PRIIPs Key Information Documents – Draft regulatory technical standards (JC DP 2015 01)

The German Banking Industry Committee appreciates the opportunity of commenting on the draft Regulatory Technical Standard (RTS) included in the Joint Consultation Paper. What we cannot understand, however, is the chosen approach: the questions put forward for consultation primarily deal with details (such as presentation issues), whilst some key aspects of the draft remain outside the scope of consultation. We would like to discuss these aspects in our introductory comments below:

1. Duty to prepare key information documents – newly-issued products, legacy products, and the secondary market

As the hearing on 9 December 2015 clearly showed, the Joint Committee assumes that, as matter of principle, products launched prior to the PRIIPs Regulation coming into force ("legacy products") will require a key information document as from the time of the Regulation being effective, unless a sale of such PRIIPs to retail customers (as defined by MiFID) can be excluded.

The strict applicability of the PRIIPs Regulation on all existing products would be highly problematic for issuers. Given that detailed Level II requirements will not be available until the first half of 2016 at the earliest, PRIIPs manufacturers will be facing significant – or even unsolvable – problems in order to prepare KIDs for newly-issued products in time. Should manufacturers be obliged to also prepare Key Information Documents for legacy products still traded on secondary markets, implementation would be virtually impossible. To better illustrate the challenge, more than a million of such products are listed on German exchanges alone. This figure clearly shows that PRIIPs manufacturers would be barely capable of preparing Key Information Documents for this mass of legacy products.

Given the immense problems involved, in practical terms, we urge the ESAs to examine, and critically re-assess their position concerning applicability for legacy products. Should this general position nevertheless remain unchanged, ESAs should consider further practical solutions – for example, limiting such applicability to products which are offered actively.

2. Problems concerning applicability of the Regulation for (OTC) derivatives used for hedging

As we pointed out during preceding consultations, many of the requirements set out in the PRIIPs Regulation fail to take the specific features of OTC derivatives into account. We therefore strongly opposed inclusion of OTC derivatives – especially where these are distributed for hedging purposes[1].

---

[1] We wrote in our comment dated 16 February 2015:
In general, we do not believe that OTC derivative transactions entered into for hedging purposes, especially in the context of interest rate and currency management, and in line with normal banking practice (especially with corporate clients), fall under the PRIIPs Regulation, given the clear definition in Art. 4 (a) of the PRIIPs Regulation and the fundamental assumptions given under numbers (6), (7), and (9) of the preamble. This is because such transactions do not constitute “investments” or “investors”, nor do they involve “early redemption amounts”. Instead,
- they constitute rights and obligations under the law of obligations, which imply payment obligations due only in the future,
- without the issuer requiring an upfront “investment” or the payment of an (investment) amount which then has to be “redeemed”; and
- in many cases, (corporate) clients would be affected, whose intention is not to effect any (cash) investments of their equity, but who want to “hedge” the risks involved in their ordinary course of business (such as currency or interest rate risks) – consider examples such as cross-currency swaps,

Furthermore, we are convinced that legislators did not consider OTC hedges when formulating the requirements.

Pursuant to Annex II, paragraph 9, certain rules for determining risk should apply to derivatives "that qualify as PRIIPs". In our understanding, this means that not all derivatives (as defined in part C, nos. 4-10 of Annex 1 to Regulation 1286/2014/EU) qualify as PRIIPs – but only those which actually fulfil the prerequisites set out in Article 4 (1) of Regulation 1286/2014/EU.

Instruments may only qualify as a "packaged retail investment product" ("PRIP") if they fulfil at least the following requirements:

- The instrument concerned must be an "investment". By definition, this requires that investors provide an amount of money and expect an "amount repayable" (cf. Article 4 (1) of Regulation 1286/2014/EU).
- The amount repayable must depend upon the performance of an underlying instrument.
- For the rules governing preparation of a Key Information Document being applicable in the first place, there must be a "manufacturer" creating a "product" that is "sold" by the manufacturer, or by a distributor (cf. Articles 4 (4), 5 (1) and 13 of Regulation 1286/2014/EU).

Numerous provisions provide an indication that the PRIIPs Regulation is not compatible at all with the special features of OTC transactions:

First of all, we need to answer the question on what level KIDs must be prepared. We believe that having to prepare Key Information Documents on a single-contract level would be disproportionate. Likewise, the requirement (as set out in Annex IV, paragraph 19) to use the nominal amount set in the respective contract for products without an initial investment needs to be abolished, since it suggests that KIDs must be prepared on a single-contract level. This would place an insurmountable burden on the sell side. Moreover, we would like to point out that the publication of individual Key Information Documents might

---

involving the *exchange* of two currencies in the future in order to hedge a future payment from an underlying commercial transaction; or an interest rate cap providing 'insurance' against interest rate changes of operating loans, etc.
Unfortunately, the present Discussion Paper does not take into account that numerous small- and mid-sized corporate clients have to be identified as “private clients" according to MiFID, but that they enter into OTC derivatives transactions for hedging (as opposed to investment) purposes. Against this background, many of the requirements now proposed for the information documents in the PRIIPs Regulation are not fit for the purpose, regarding such hedging transactions.
Thus, OTC derivative transactions carried out for hedging purposes in the context of interest rate and currency management, in line with normal banking practice, feature special characteristics which are not reflected in the Discussion Paper at all. The result is PRIIPs requirements that cannot be implemented in this line of business. For example, regarding the presentation of risk, all of the featured calculations generally require that an actual investment be made, including physical redemption to the customer. However, no indications are made in this context regarding potential requirements for OTC derivatives – this issue remains unreflected.
We therefore request clarification in the Paper that OTC derivative transactions entered into by corporate clients for hedging purposes (in the context of interest rate and currency management, and in line with normal banking practice) be exempt from PRIIPs-related requirements.

disclose sensitive data concerning the specific details of agreements between contracting parties; given that a part of such details would disclose business secrets, this would be very difficult to explain to clients. We would also like to draw your attention to the fact that the other provisions in the draft RTS concerning the contents of a KID, and the limitations placed on the number of pages, prevent a sensible generic description of the product concerned. For this reason, we are unable to follow the invitation, communicated during the Joint Committee hearing to the draft RTS on 9 December 2015, to provide suitable proposals for OTC derivatives. Further clarification from ESAs will be required concerning the following areas:

- Details concerning sample investment volumes and redemption scenarios for OTC derivatives will be incorrect, or even misleading, in most cases. In contrast to securities with a large number of investors, it is impossible to standardise individual contracts, with highly customised hedging periods and amounts hedged, in any sensible manner. Having to provide such details would expose manufacturers to significant and disproportionate liability risks, and would lead to the threat of providers withdrawing from this business.
- Providing a KID in good time (recital 19 and Article 12 of the PRIIPs Regulation require that all persons advising on, or selling PRI(I)PS provide a KID to the client in good time before **each** transaction is concluded) is generally inconsistent with standard practice in the financial sector, and is out of line with the requirements of business clients in foreign exchange trading: business clients (classified as retail customers) usually call without giving advance warning, and wish to execute their foreign exchange transaction on the phone, without any delay, in order to avoid exchange rate disadvantages. Moreover, an increasing number of clients conduct their foreign exchange business via online trading platforms, where the bank only notices such client trading activity at the time of a trade being executed. As with OTC trades, this highlights the fundamental issue as to how time-critical transactions – which are a regular occurrence in this context – should (or may) be handled.
- We see another significant problem regarding KIDs for OTC derivatives on a single-contract level, in the requirement for a new KID to be prepared in the event of material changes. The problem here is that the risk assessment of OTC transactions generally depends upon prevailing market circumstances – therefore, most market fluctuations may have a direct impact upon KID details. Hence, the exception ("KID revision only for material changes") is likely to quickly turn into the rule.
- Where customised OTC transactions are involved, the obligation to publish the KID on the issuer's website would lead to excessive documentation duties – which would lead to further delays in entering into a transaction.
- Likewise, the risk indicator fails to incorporate the purpose of an OTC derivatives contract. From a risk-assessment perspective, OTC derivatives linked to an underlying transaction and used for hedging purposes cannot be treated in the same way as OTC derivatives used for speculation.

In our opinion, expanding the scope of application to include OTC derivatives used for hedging would be highly disproportionate. It is for good reason that the European Market Infrastructure Regulation (EMIR) includes a specific differentiation between OTC derivatives used for hedging and those used for speculative purposes, whereby both the bank offering the contract and the corporate client must report on the nature of the transaction (cf. Regulation 148/2013, Annex, Table 1, reporting field 15). This ensures the targeted distinction for such customised agreements. The special nature of OTC derivatives used for hedging is also evident in the fact that, pursuant to Article 10 (3) of EMIR, OTC transactions used for hedging are excluded when determining mandatory clearing thresholds for non-financial counterparties; this accounts for the specific risk assessment of these transactions. Furthermore, recital 31 states: "[...] When the clearing threshold is set, the systemic relevance of the sum of net positions and exposures per counterparty and per class of OTC derivative contract should be taken into account. In that connection, appropriate efforts should be made to recognise the **methods of risk mitigation** used by non-financial counterparties **in the context of their normal business activity**."

The German Banking Industry Committee would like to point out that an estimated 95% of OTC derivatives business in Germany is entered into with corporate clients. For some institutions, two-thirds of these corporate clients would need to be classified as private customers according to MiFID. Virtually all foreign exchange and interest rate derivatives are entered into for hedging purposes.

In addition, a typical German SME conducting import/export business with non-euro countries enters into very similar transactions on a repetitive basis: usually, only the amount hedged and the term of the transaction differ. As a consequence, the burdens outlined above would have a particular impact, without creating any added value whatsoever for the company.

As the evolution of EMIR, and in particular, the G20's declared – and as yet unachieved – goal of forcing more OTC derivatives to mandatory clearing (EMIR) and on regulated markets (MiFIR) have shown, a far-reaching standardisation of these contracts is a very difficult task.

We would like to once again entreat European authorities, in the strongest possible terms, to outline its position concerning the scope of application, and to substantiate *why* they consider OTC derivatives to be within that scope, according to the wording of the Regulation. In spite of repeated requests put forward by stakeholders, ESAs have not provided any additional information, nor have they sought to consult stakeholders.

Should there be a need for further regulation concerning the disclosure of information to contracting parties of OTC derivatives used for hedging purposes, the German Banking Industry Committee strongly believes that such regulations must be dealt with in a separate legislative process.

3. Interconnections with MiFID II

It should be noted that there are strong thematic interconnections between some of the new investor protection rules in MiFID II - such as cost disclosure, performance scenarios, target market and some other specific product governance requirements - and PRIIPs. We would therefore like to draw urgent attention to the fact that a decision to delay implementation of the MiFID II investor protection rules would have strong implications for PRIIPs as well, and would in all likelihood result in manufacturers not having sufficient clarity on all content details for the purposes of providing all required KIDs before the end of next year.

4. Comments to the draft Delegated Regulation

a) "Identity" section, Art. 3

Pursuant to Article 3 f), the Key Information Document should include the date of creation and of any subsequent amendment. This exceeds the requirements set out in the Regulation: pursuant to Article 8 (3a), the Key Information Document only needs to contain the date on which it was created. This means that in the case of a revised Key Information Document, stating the date of the revised (and hence, re-created) Key Information Document will be sufficient. The Regulation does not require to state the dates of previous Key Information Documents. Likewise, Article 10 does not state such a requirement; it is decisive that a revised document complies with the requirements set out in the Regulation. Moreover, previous documents are not relevant for an investment decision taken by the investor. Article 3 f) of the

Level II Regulation should be worded as follows: "...the date of the latest revision of the key information document."

b) "What is this product?" section, Art. 4

Pursuant to Article 4 (4), the KID should include details concerning the target market as defined in MiFID II. We strongly welcome this, given the importance of consistency with MiFID II, to the extent that the respective scope of application is concerned. Unfortunately, the requirements do not contain any clear cross-reference to the related MiFID II provisions; instead, it states criteria for determining the target market – however, there is strong reason for doubt as to whether individual aspects (e.g. the concept of "knowledge") are relevant for target market determination in accordance with MiFID II. In order to avoid any discrepancy of assessments, relative to the criteria set out in MiFID II, Article 4 (4) should only contain a simple cross-reference to the target market determined in accordance with Article 16 (3) of MiFID. The specification of target market requirements should be seen exclusively in connection with MiFID II – mainly because the MiFID II requirements go beyond the pure statement of a target market; these rules have an immense impact in terms of practical implementation. Moreover, market participants are already deeply involved in implementing MiFID II; there is a serious threat of this work now being thwarted by new (and diverging) requirements. Apparently, ESMA is already looking into this issue, as part of possible Level III measures.

c) "Other relevant information" section, Art. 11

According to Art. 11 (3) PRIIPs that are available to retail investors shall include the statement that the KID is updated at least every 12 months. We assume that for most KIDs no update is required. In such cases, the statement that the KID is updated at least every 12 months would be misleading. We suggest a deletion of that requirement.

d) Review, revision and republication of the Key Investor Document – Chapter IV

It is important to clarify in which situations a Key Information document needs to be updated/revised. Until now the Draft Regulatory Technical Standards do not provide any answer on that issue.

The provision in Article 18 does not provide any guidance on how to deal with a Key Information Document that needs to be revised. For the sake of legal certainty, a clarifying rule should be included whether an existing Key Information Document may continue to be used until publication of an updated version (provided that the other conditions are met, i.e. revision and publication without undue delay).

Recital 19 provides for the option of issuers informing existing investors by e-mail (mailing list or e-mail alert) in the event of Key Information Documents being revised. This option is hardly compatible with the nature of KIDs as pre-contractual information, since it would no longer be possible to fulfil their purpose on an ex-post basis. Implementation would also involve disproportionate additional expenditure. Therefore, this clause should definitely be deleted.

e) Article 20 is shown twice

The present draft contains two clauses named "Article 20" ("PRIIPs made available in a non-continuous manner" and "Conditions on good time"). This should be fixed in the final version.

5. Template of the Key Information Document (KID), Annex I

We have serious doubts as to whether all the information provided for will in fact fit on three pages, as set out in Article 6 (4) sentence 1 of the PRIIPs Regulation – especially given the fact that two overviews are required for the cost overview alone, with additional explanations required to the overview of risks, as well as for the performance scenarios. We believe that practical tests must be carried out prior to finalisation of the RTS, with an additional examination as to which parts of the KID may be dropped.

Further practical tests would also have the advantage, that the publication of “best practices” would increase legal certainty for manufacturers. If the ESAs should adhere to the opinion that derivatives fall within the scope of the Regulation, this would be of particular importance for the process of drawing up KIDs for OTC derivatives. As we have pointed our above, many requirements are not compatible with the special features of OTC derivatives. Therefore, best practices might give an indication, how to deal with these problems.

6. “What are the risks and what could I get in return?" section, Art. 5, Annex II & III

We support the Regulation's overarching objective to achieve comparability among all PRIIPs. As already pointed out in our statement dated 24 August 2015, the German Banking Industry Committee takes a critical stance regarding the different ways in which market risk is derived: an objective comparability of product-specific risks cannot be guaranteed in this manner. We would consider this a significant breach of Level I requirements.

Therefore, the German Banking Industry Committee has advocated applying a uniform risk-assessment method across *all* packaged products, thus creating a permeable risk classification system. This is the only way to avoid competitive distortions between different product types, and to inform retail investors in an appropriate way, prior to their investment decision. In any case, the current proposal requires modification.

The purpose of the Summary Risk Indicator prescribed in Article 8 (3) (d) of Regulation (EU) 1286/2014 is to allow retail investors a sound assessment of risks the product is exposed to, and to enable them to compare packaged products.

However, initial calculations show that a large number of packaged products is assigned to the highest risk classes. For instance, certain equity funds as well as diversified equity investments (such as those linked to the EURO STOXX 50 index) assigned to class 7 are considered to be equally risky as a leveraged knock-out certificate, for example. As a result, retail investors who are *per se* relatively risk-averse will be discouraged from investing in an equity fund – even though the fund's actual risk exposure might in fact be compatible with the investor's investment profile.

The lack of differentiation of risks involved in relatively more risky financial instruments is a problem especially for conservative investors who tend to be risk-averse – the Final Report "Consumer testing

study of the possible new format and content for retail disclosures of packaged retail and insurance-based investment products" identifies conservative investors as a typical type of investor (page 61). Experience gained by banks and savings banks in investment advisory services has shown that especially during the persistent low-interest rate environment, investors are looking for higher-yielding forms of investment – at a risk exposure they consider acceptable. Of course, equity funds are a suitable – if not indispensable – investment product for conservative investors with a correspondingly long investment horizon. Given that the current proposal does not allow for any differentiation – and hence, for an adequate assessment by investors in products exposed to relatively higher risks – retail investors with a relatively lower risk appetite may be discouraged from investing in equity funds. This is not just counter-productive to the political goal of investor protection; it also runs counter to efforts to raise the equity market propensity of retail investors in a European Capital Markets Union.

The lack of differentiation may have several causes which may be interconnected. It is obvious that the proposed volatility scaling for the purpose of allocation to MRM classes 1 to 7 is relatively granular whilst the classification in the higher risk classes is based on relatively large intervals. In this context, it is worth noting that this risk interpretation (which we believe to be inappropriate) was not subject to consultation in the discussion paper dated 17 November 2014.

We therefore propose the following adjustment to risk scaling, in order to achieve a more differentiated risk classification:

MRM class	Proposed thresholds*	JC thresholds*
1	< 2.5%	< 0.5%
2	2.5%-5%	0.5%-2%
3	5%-15%	2%-5%
4	15%-25%	5%-10%
5	25%-35%	10%-15%
6	35%-45%	15%-25%
7	> 45%	> 25%

* thresholds for annualised volatility

We would like to draw attention to our impression that the Joint Committee is hastily cobbling together a concept. This is reflected in particular in corrections of the formulae and the missing consultation of major aspects of the new risk assessment method. It is highly inappropriate, given the importance of this issue – also with regard to potential allocation effects on the real economy over the long term.

Please refer to our comments to item 2. regarding the particularities of determining risk exposure of OTC derivatives used for hedging purposes.

Finally we are of the opinion that the explanations given in Appendix 1 to Annex III should be facultative.

7. Performance Scenarios, Annex IV and Annex V

The approach proposed in the Consultation Paper requires the scenarios primarily to be based on the "recommended holding period" (which could be something like "five years"). We consider this approach to be wrong: any scenarios based on periods which are shorter than the product's recommended holding period or final maturity are unsuitable for providing transparent information to investors. This is due to

the fact that such scenarios are based on numerous assumptions, with each scenario having an extremely small probability. The structure and special features of packaged investment products is thus not taken into consideration.

Moreover, for products with a fixed maturity date, the recommended holding period would often not correspond to the maturity date. This would mean that the scenarios would, in the absence of payouts under the products before their maturity dates, have to be calculated based on exchange (or OTC) prices. In addition, two other scenarios would have to be displayed for shorter holding periods. At least for structured securities, scenarios on this basis would be highly problematic from a methodological perspective. Instead, for products with fixed maturity dates, only one performance scenario should be required for that date. Generally, three scenarios would be required. However, and differing with regard to the practice for certain national law product information documents (like the German Produktinformationsblatt), the middle scenario would be called "moderate", and would have to be calculated based upon the expected return. This kind of approach appears doubtful from a methodological perspective, as it could mislead investors into expecting the realisation of that scenario with a high degree of certainty. In addition, it could let certain product structures appear generally unappealing; depending on prevailing market conditions, it could seem that only "long" or "short" products would make sense to invest in at certain points in time. This would make a comprehensive product line that met all investor market expectations difficult to defend.

A better way would be to allow the "moderate" scenario to be set freely according to reasonable discretion of the issuer, or to turn this into a "neutral" scenario - like in the German PIB - where investors neither win nor lose. In addition, it should be possible to include more scenarios, if the structure and functioning of the product cannot be fully captured by three such scenarios.

Moreover, we see the proposal of defining further requirements at Level III (pursuant to Article 6 (7) of the draft scenario definitions) as very critical, since it will further complicate implementation of requirements – which is already very critical in terms of timing. For this reason, detailed specifications should be set out directly at Level II, and should not be deferred to Level III.

We see another problematic issue in the requirement for an additional performance scenario to be included, pursuant to Article 6 (4) of the draft Delegated Act, if a covered insurance event occurs. This option is a contravention to the requirement concerning cost disclosures, according to which not all costs involved in hedging risks must be listed (at least for biometric risk premiums). To avoid competitive distortions, a uniform procedure should be agreed upon: either, biometric risk premiums remain completely unaccounted for (meaning that neither associated costs or added value are shown), or both aspects are included in KIDs – in which case costs would need to be fully accounted for as well.

The fact that, pursuant to the provisions of Annex IV, section 18 of the draft Delegated Act, different assumptions are to be used regarding investment amounts gives cause for concern regarding potential competitive distortions at the expense of PRIPs. Given that scenarios for PRIPs are to be calculated using a nominal investment amount of €1,000, whilst scenarios for insurance products are supposed to be calculated on the basis of an investment amount of €15,000 (or an annual amount of €1,000), returns for PRIPs would be lower in absolute terms. To prevent such distortions, and in order to facilitate the desired product comparisons, a uniform notional amount of €10,000 should be used as a basis for all product types. This amount would be closer to actual order sizes, providing a more realistic picture of expected returns to investors. For example, the members of a large industry association have recorded average

order sizes of €7,272 for warrants and €9,694 for certificates. Looking at investment funds, a large German provider has indicated to us that one-time orders average approximately €8,500.

Finally, the requirement to provide separate explanations concerning scenario presentations (cf. page 56, last item) will result in significantly higher efforts for issuers. Therefore, this requirement should be deleted altogether, or should be made optional.

The handling of products with a short remaining term is also unclear: a clarification should be provided that indications regarding interim dates may be waived.

For the avoidance of doubt, we would like to point out that all our comments below, which refer to our comments to item 2, do not refer to OTC derivatives.

8. Methodology for the calculation of costs, Annex VI and Annex VII

The Consultation Paper is not fully consistent on this topic. For example, there are differences with regard to the treatment of hedging costs (general definition of "fair value" on the one hand; explicit requirement for this to be counted as cost, on the other). Also, the Consultation Paper implies that the fair value should correspond, for each product, to the value reported in the balance sheet of the issuer. However, the issuer's balance sheet does not show the value of all individual products issued.
The proposed treatment of spreads probably needs to be readjusted at least partly (depending on the outcome of the detailed assessment of cost disclosure jointly under PRIIPs and MiFID II - discussions within the industry ongoing).

Furthermore, the holding period assumed for the presentation of costs would need to be aligned with the holding period used for performance scenarios (in case of its amendment as suggested above, using the fixed maturity date).

Given that KIDs are documents prepared within the manufacturer's sole responsibility, it is indispensable that any cost items listed are the manufacturer's costs – and hence, known to the manufacturer.

In addition, consistency between the PRIIPs requirements and the transparency requirements pursuant to MiFID II concerning product-related costs is indispensable.

The requirement that PRIPs-related costs be calculated based on an investment amount of €1,000 (compared to an investment amount of €15,000, or €1,000 per annum), as set out in Annex VI, no. 85, is a problem, since it distorts the presentation and may lead to competitive disadvantages for the products concerned. In order to facilitate the desired product comparisons, a uniform investment amount of €10,000 should be used as a basis for all products. This amount would be closer to actual order sizes, providing a more realistic picture of expected costs for investors. For example, the members of a large industry association have recorded average order sizes of €7,272 for warrants and €9,694 for certificates. Looking at investment funds, a large German provider has indicated to us that one-time orders average approximately €8,500.

For the avoidance of doubt, we would like to point out that all our comments below, which refer to our comments to item 2. do not refer to OTC derivatives.

Comments to the Joint Consultation Paper PRIIPs Key Information Documents – Draft regulatory technical standards (JC DP 2015 01)

Question 1
Would you see merit in the ESAs clarifying further the criteria set out in Recital 18 mentioned above by way of guidelines?

As we outlined in our introductory remarks, the remaining time for implementing the requirements of the PRIIPs Regulation is so tight that we do not see any possibility for the implementation of more specific details in the form of guidelines. Any additional requirements would (further) threaten the timely implementation. Therefore, this proposal should not be pursued any further.

Question 2
1. *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?*
2. *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?*

(i) We cannot reconcile the proposal of applying different assumptions for certain product groups. This is a contradiction of European legislators' objective to create uniform Key Information Documents for the investment products concerned, with a view to enabling product comparisons across the various product groups. The only way to reach this objective is to apply uniform assumptions to the contents of Key Information Documents. Failing this, Level II specifications run the risk of undermining the objectives of Level 1 legislators.
We see the additional threat of differing assumptions leading to a disadvantage for certain products such as PRIPs: for instance, a higher investment amount (such as the one prescribed for insurance-based investment products) may regularly lead to a higher return in absolute figures. Amounts should therefore set in order to provide a realistic picture for 'typical' investors – in other words, the amounts should be based on realistic order sizes. Uniform assumptions should definitely be applied in order to prevent the outlined consequences. An amount of €10,000 appears to be appropriate. For example, the members of a large industry association have recorded average order sizes of €7,272 for warrants and €9,694 for certificates. Looking at investment funds, a large German provider has indicated to us that one-time orders average approximately €8,500.

(ii) Indeed, an exception should be permissible for PRIIPs with a fixed investment amount, allowing manufacturers to use this amount as a basis. However, since such a customised specification involves significant efforts, this approach must be provided as an option only.

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?

Tests were showing that both methods are leading to similar results. Due to the fact that the bootstrapping approach is far more complex, we are supporting the Cornish Fisher expansion.

Comments to the Joint Consultation Paper PRIIPs Key Information Documents – Draft regulatory technical standards (JC DP 2015 01)

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.

Whilst the confidence interval is an element of the VaR formula, and hence, part of the calculation basis for VaR-equivalent volatility (VEV), in essence, its level is only of lesser importance.
An aspect that we consider to be far more critical is the fact that the calculation formula does not consider the current product risk, but the risk at the end of maturity. This is resulting in non-comparable results for products with different maturities.

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?

No answer.

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?

No answer.

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?

Referring to the credit risk assessment proposed in the CP, a further adjustment for tenors seems not to be a sound approach, since the tenor already influences the MRM of the PRIIP. Of course, credit risk - in general - increases with longer tenors, but there is no linear relation to the credit risk, so such an adjustment could produce misleading results. In an alternative approach that we propose, the credit risk relies on the tenor (see answer to question 8).

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.

Referring to the MRM we believe that the scale is too conservative by a considerable degree, and does not reflect the investment reality. According to the proposed methodology for the SRI, popular standard investments fall into the highest risk categories. From our point of view, a well-diversified equity investment (e.g. EURO STOXX 50 index) should be allocated somewhere in the middle of the classification scheme in order to allow a differentiation among different PRIIPs. With the proposed scheme, these investments are allocated in the highest risk classes.

Referring to the CRM we are of the opinion that the gap of 2 SRI classes resulting from a one notch rating difference is not meaningful. In practice, a capital guaranteed structure from an A issuer (S & P scale) would have an SRI of 1 (MRM 1, CRM 2) while the same product from a BBB rated issuer would be allocated in SRI class 3 (MRM 1, CRM 3). The gap of 2 classes is not comprehensible at all.

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?

This approach seems to be reasonable for investors who buy a product at 100% of the nominal (e.g. primary market). In case the investor purchases a product later through the secondary market he may pay e.g. 120% of the nominal, since market performance may increase the value of the product. This investor does not get 100% capital protection but only a partial protection. Therefore, there should be a difference between primary and secondary market for the MRM. The tenor is relevant because of the price impact of duration. If there is a secondary market, the tenor is irrelevant because the market risk has to be taken into account anyways. And if there is no secondary market the tenor may not generate a price impact. At the end, the tenor is irrelevant in both cases.

In essence, determining SRI using different (qualitative and quantitative) methodological approaches means that retail investors cannot objectively compare product-specific risks.

This is why a uniform method, incorporating all product features, should be applied: this might be achieved, for example, by calculating risks on a VaR basis, applying a uniform holding period across all products.

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?

No answer.

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?

The methodology as set out in Annex II, paragraph 55 c) would mean that in case of a structured bond on the DAX the credit assessment should include all companies being covered by the DAX. Since credit risk of those companies is not relevant (barely measurable) the logic should be that as long as the payout is linked to performance, then credit risk of the underlying should not have any impact. Therefore, this article should be deleted.

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?

The currency risk depends on the home currency of the investor. Since the PRIIP-KID should be the same in all countries, it is not possible to have a general integration of the currency risk into the SRI calculation. However, a general disclaimer could be added, giving investors a hint that they should be clear about the currency of their investment - and that they should be aware that there could be a currency risk in case the product's currency was not their home currency.

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?

No, please refer to our answer to question 9. These products could be treated the same way as Category III products.

It is correct that some products have a significantly higher risk approaching final maturity. Risk classes for different holding periods could illustrate the risks for different holding periods. As these calculations are also (and already) requested for scenario analysis, there is no additional effort. Given that retail clients typically do not perceive narratives as relevant as graphical illustrations, we recommend using an additional figure. Compared to the well-designed presentation of the cost indicator, the presentation of the SRI is still simple and allows disclosure of additional graphical information.

As pointed out in our previous answers (especially in response to question 9), the problem of lower risk at the end of maturity (compared to shorter horizons) only arises because of the end of maturity perspective.

In addition, it does not allow a comparison between different PRIIPs, which counters a central aim of the regulation. This could be adjusted by changing the end of maturity perspective into a prescribed holding period approach for calculating the SRI. An appropriate, consistent holding period for instance could be one year, which is also used in other regulatory frameworks (e.g. Basel III). It is obvious that such a consistent holding period is not appropriate for each and every retail investor / PRIIP, but this can be ignored due to the fact that the calculated risk figure / the VEV only serves as a technical basis for deriving the overall SRI. The same applies with the current methodology, because of the transformation of the end of maturity Value at Risk into an annualised volatility equivalent. In conclusion, the risk figure / VEV itself cannot be taken as a realistic value for the product risk.

Therefore, we strongly recommend using one approach and one holding period, in order to ensure comparability and potential risk changes during a holding period. Such a methodology also takes into account the maturity of the product by reflecting all relevant risk factors (besides price risks, also interest

rate risk, volatility risk etc.) in the calculation of the SRI. Such an approach was outlined in option 3 in the technical discussion paper, and is well-established for many PRIIPs across Europe.

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 would like to point out that the final version of a draft RTS must include specific cross-references to the sections the RTS refers to (including the exact section referred to). The reference contained in Annex IV (17) ("[cost section on performance fee]") is so unspecific that it may lead to interpretation issues in practice.

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?

We consider the table overview in Annex V to be clearly more transparent than the graphic display; for this reason, the table should be used.

By no means should both versions be used: repeating identical statements in an additional overview would only confuse investors, and would not provide any added value. Moreover, this raises the issue (as stated several times already) whether the prescribed contents will actually fit within the three-page limit provided in Article 6 (4) sentence 1 of the PRIIPs Regulation. This issue would likely exacerbate if certain content was to be listed twice.

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 generally welcome the approach of determining transaction costs using standardised estimates. However, it is vital that such estimates are reviewed on a regular basis, and adjusted if necessary.

This approach should not only apply to newly-launched funds, but also for existing ones. Since in practice, fund management companies will hardly be able to consistently calculate transaction costs, these should also be determined using estimates for existing funds.

Comments to the Joint Consultation Paper PRIIPs Key Information Documents – Draft regulatory technical standards (JC DP 2015 01)

With regard to the calculation of transaction costs for investment funds we deem it 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. 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. Hence, the data published by Bloomberg "all quotes" do not represent adequate mid-market prices of fixed-income investments. It is imperative that calculations on the basis of such prices of a purely indicative value will always entail faults and in any case, are not capable of establishing real transaction costs for fixed-income trades.

MiFID II might remedy this situation in the longer term due to the new requirements for pre-trade transparency applicable to fixed-income instruments. However, with the probable postponement of MiFID II entry into force, it is clear that the necessary data will not become available in time for the implementation of the PRIIPs KID requirements. Even without a formal postponement of MiFID II, from a today's perspective it is difficult to assess whether the new pre-trade transparency regime will result in the effective access to market prices or whether the current market fragmentation will prevent such data consolidation and availability for the buy-side. In any case, it is far too early to expect fund managers to make calculations on the basis of data which the market is yet to deliver. Therefore, we believe that the ESAs would be best advised to revive the hybrid approach to the calculation of transaction costs which has been favoured in the previous round of consultation. Under this approach, implicit transaction costs embedded in fixed-income prices should be calculated by reference to a standardised table established by the ESAs.

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)

We generally agree with the view that standardised values need to be reviewed on a regular basis. Given the implementation deadline, which is already very tight, these values should initially be determined at Level II. In any event, estimated values should not be determined via guidelines, since this would further shorten the timeframe for implementation – which can only commence once all requirements have been set.

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)?

From our point of view, presenting annualised values is more convincing, in particular since this reflects the relative decline in one-off costs. Moreover, monetary values would also be consistent with the

percentage disclosure of RIY, which also declines over time. If the 'summing up-method' were used, investors would hardly be able to reconcile why total costs shown in absolute figures keep rising (given the summing-up) whereas the RIY, which is expressed as a percentage, falls.

However, if the presentation is based on annualised values, it must be ensured that this is made sufficiently clear.

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?

From our point of view, when calculating the fair value of biometric risk premiums, the minimum requirement is to ensure that there is no leeway for overestimating fair value. Since the costs embedded in the fair value need not be included in the total costs, there may be an incentive to estimate such costs as high as possible, and to reduce costs to be disclosed accordingly. This would distort the disclosure since costs would then be shown to be lower than they really are.

We would also question whether it is really necessary to exempt the fair value of biometric risk premiums from total costs. After all, it is possible to show the related added value elsewhere – in the product description, for example. If this option is available, we see no reason for factoring out a part of the costs. A consistent approach is called for here: either full costs should be disclosed, together with the added value – or none of the two factors should be shown.

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?

The way we understand the requirements in Annex VI, paragraph 55, on calculating the costs of biometric risk premiums, only the difference between premium payments and fair value is included in the total costs. However, if fair value is not factored into the presentation of costs, it should also not be emphasised in another context: this would mean that the KID presents the added value associated with fair value – but not the associated costs.

In our opinion, fair value should only be presented if the related costs are also fully included in the total 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?

First of all, we see the fundamental issue whether the second table is necessary at all. In this context, we would like to stress a general problem raised several times: we have serious doubts as to whether it is sensible to show four different tables (together with additional information) on just three pages. In the case at hand, it is also worth noting that Level I rules do not require any further breakdown of costs, and that the added value of such a presentation is likely to be marginal. The second table should therefore be left out altogether.

If, however, retaining the second table is nevertheless considered sensible, the costs associated with individual items should be shown in monetary amounts, since most investors are hardly able to reconcile percentage disclosures.

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?

From an investor's perspective, having several tables in the KID should not present a problem *per se*. On the contrary: since the presentation of performance scenarios and costs follow the same logic to some extent, presenting information in the form of tables is a sensible approach. Investors who have understood the logic of using three points in time for the performance scenarios will also grasp the logic of disclosing costs in the same form.

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?

Most investors will likely need supplementary explanations in order to fully understand the presentation of performance fees – yet there is insufficient space to provide such explanations. For this reason, we consider the proposal to be inappropriate. In case this information should be deemed as necessary, the graphic should show costs on a per-annum basis.

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?

In principle, we would welcome combining both tables, since this would require less space. However, this would lead to a level of complexity of the combined table that would hardly be transparent to investors. For this reason, we would once again like to suggest deleting the second table.

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?

No answer.

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?

If costs were nonetheless presented in the form of two tables – as opposed to our suggestion, we would indeed welcome leaving out the breakdown in the "costs over time" table, since this is somewhat redundant given the more extensive breakdown in the "composition of costs" disclosure. Moreover, a reduced presentation would save considerable space, which we would welcome especially in view of the limited space available in KIDs.

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.?

The breakdown should include all cost information on the financial instrument which may be relevant to comply with MiFID II.

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.

No answer.