European Securities and Markets Authority

Reply form for the Technical Discussion Paper on PRIIPs

23 June2015

European Securities and Markets Authority

Date: 23 June 2015

Responding to this paper

EBA, EIOPA and ESMA (the ESAs) welcome comments on this Technical Discussion Paper on Risk, Performance Scenarios and Cost Disclosures in Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs).

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response so as to allow them to be processed more efficiently. Therefore, the ESAs will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
- do not remove the tags of type < ESMA_QUESTION_PRIIPs_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
- if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that the ESAs should consider

Naming protocol

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESA_TDP_PRIIPs_NAMEOFCOMPANY_NAMEOFDOCUMENT.

E.g. if the respondent were XXXX, the name of the reply form would be:

ESA_TDP_PRIIPs_XXXX_REPLYFORM or

ESA_TDP_PRIIPs_XXXX_ANNEX1

To help you navigate this document more easily, bookmarks are available in “Navigation Pane” for Word 2010 and in “Document Map” for Word 2007.

Deadline

Responses must reach us by **17 August 2015.**

All contributions should be submitted online at www.esma.europa.eu under the heading ‘Your input/Consultations’.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with the ESAs' rules on public access to documents.[1] We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Board of Appeal of the ESAs and the European Ombudsman.

Data protection

Information on data protection can be found on the different ESAs' websites under the heading 'Legal notice'.

[1] See https://eiopa.europa.eu/about-eiopa/legal-framework/public-access-to-documents/index.html.

General information about respondent

Name of the company / organisation	Society of Actuaries in Ireland
Activity	Insurance and Pension
Are you representing an association?	☒
Country/Region	Ireland

Introduction

Please make your introductory comments below, if any:

< ESMA_COMMENT_PRIIPs_1>

The Society of Actuaries in Ireland ("SAI") welcomes this Technical Discussion Paper ("the Paper") and appreciates the level of consultation being carried out under the PRIIPs implementation process.

The SAI has some overall comments on the paper as follows:

- The current proposals in this Technical Discussion Paper are trying to cover all types of product. We believe that this is appropriate. However some of the proposals are there to address very complex products which are likely to be a small proportion of the products sold. On considering this Paper, we believe that it would be appropriate to use the classification of "complex" proposed in the PRIIPS legislation to ensure that that more complex solutions proposed are applied to these products only. The majority of the products would be subject to rules on the simpler end of the scale. So for example, a model specified by the regulator could be used for "normal" funds (e.g. ETFs, unit linked funds, simple structured products where outcomes are expected to be linear). The complex solutions should be used for the complex products.

- The SAI believes that complexity in models should be avoided where possible. There is a saying that "All models are wrong but some models are useful". We believe that the objective should be a simple model which demonstrates the risks and enables them to be understood by the consumer. We should avoid complex models that are costly to implement and maintain and contain an illusion of precision.

- For "non complex" products we believe that the regulator should specify a simple stochastic projection model and parameters and also provide tables of the percentiles. This means that for simple products, the manufacturer can simply apply the table. For complex products, the actual stochastic model can be used. Furthermore we believe that where this model is not appropriate, the manufacturer should supplement the information with "what if" scenarios. The onus should be on the manufacturer to demonstrate that the model is appropriate and be prepared to defend its decision not to show supplemental scenarios.

- We believe that the risk indicators should be as consistent as possible with those used in UCITS (i.e. grades 1 to 7) to enable comparisons with UCITS and avoid "reinventing the wheel". Of the options listed, we would favour Option 2 but would prefer to see a qualitative measure of credit and liquidity risk.

- In relation to costs disclosed, we believe that there should be consistency with UCITS as much as possible. However we support the reduction in yield proposal as we believe this is much more meaningful than alternatives and has worked well to date in Ireland.

- We believe that financial guarantee costs and costs of biometric risks should be disclosed and included in the RIY calculation. However these costs should be separated out. For example, “RIY is x% of which y% is for guarantee costs and z% for biometric risks.”

- One of the major issues raised by the last consultation was in relation to multiple fund choices within one product. We note that this has not been dealt with in this consultation but we would be keen to understand the latest thinking on this.

< ESMA_COMMENT_PRIIPs_1>

1. Please state your preference on the general approach how a distribution of returns should be established for the risk indicator and performance scenarios' purposes. Include your considerations and caveats.

<ESMA_QUESTION_PRIIPs_1>

(a) This is the most objective and is well established for UCITS.

<ESMA_QUESTION_PRIIPs_1>

2. How should the regulatory technical standards define a model and the method of choosing the model parameters for the purposes of calculating a risk measure and determining performance under a variety of scenarios?

<ESMA_QUESTION_PRIIPs_2>
A simple stochastic model should be prescribed. In addition, a table showing a range of percentiles for projected performance for each major asset class. This table should be consistent with the stochastic model outputs. Manufacturers can use the table or the stochastic model to provide projected returns. It would be envisaged that the stochastic model would be used for only more complex products. Manufacturers should be required to consider whether the model is appropriate and where not provide further projections or scenarios to show the risks. The model should be prescribed and model and parameters should be set by a supervisory authority
<ESMA_QUESTION_PRIIPs_2>

3. Please state your view on what benchmark should be used and why. Are there specific products or underlying investments for which a specific growth rate would be more or less applicable?

<ESMA_QUESTION_PRIIPs_3>
Inflation
<ESMA_QUESTION_PRIIPs_3>

4. What would be the most reasonable approach to specify the growth rates? Would any of these approaches not work for a specific type of product or underlying investment?

<ESMA_QUESTION_PRIIPs_4>
Risk premiums should be used where appropriate. However we believe the risk premiums should gradually move to long term average over the longer term projections as there would be greater uncertainty.
<ESMA_QUESTION_PRIIPs_4>

5. Please state your view on what time frame or frames should the Risk Indicator and Performance Scenarios be based

<ESMA_QUESTION_PRIIPs_5>
Intermediate time frames should be shown as well as the time frame for the recommended holding period
<ESMA_QUESTION_PRIIPs_5>

6. Do you have any views on these considerations on the assessment of credit risk, and in particular regarding the use of credit ratings?

<ESMA_QUESTION_PRIIPs_6>
Credit risk should be shown separately. Credit ratings should be used. However the onus should be on the manufacturer to demonstrate that the use of credit ratings is appropriate.
<ESMA_QUESTION_PRIIPs_6>

7. Do you agree that liquidity issues should be reflected in the risk section, in addition to clarifications provided in other section of the KID?

<ESMA_QUESTION_PRIIPs_7>
Yes
<ESMA_QUESTION_PRIIPs_7>

8. Do you consider that qualitative measures such as the ones proposed are appropriate or that they need to be supplemented with some quantitative measure to some extent?

<ESMA_QUESTION_PRIIPs_8>
The qualitative measures are appropriate. Cost and exist penalties should be considered where there are genuine penalties for lack of liquidity rather than simple charges. These should be covered in the narrative.
<ESMA_QUESTION_PRIIPs_8>

9. Please state your views on the most appropriate criteria and risk levels´ definition in case this approach was selected.

<ESMA_QUESTION_PRIIPs_9>
If this option was taken, we believe that it should be aligned with the UCITS criteria as much as possible (i.e. 7 indicators rather than 5) and use the same methodology as UCITS (volatility etc.). This would enable comparability with UCITS investments.
<ESMA_QUESTION_PRIIPs_9>

10. Please state your views on the required parameters and possible amendments to this indicator.

<ESMA_QUESTION_PRIIPs_10>
Of the options available, we believe Option 2 is the most suitable. However for structured products we would favour using the same approach as UCITS for comparability and consistency.
<ESMA_QUESTION_PRIIPs_10>

11. Please state your views on the appropriate details to regulate this approach, should it be selected.

<ESMA_QUESTION_PRIIPs_11>
We would not favour Option 3 due to the costs involved and the potential difficulties understanding this approach. Also, various studies (e.g. “Developing a Risk Rating Methodology” Clare 2010) have shown that historic volatility is a far better predictor of risk than other measures. Should this approach be taken, we believe the parameters/model should be set down by regulators. <ESMA_QUESTION_PRIIPs_11>

12. Please state your views on the general principles of this approach, should it be selected. How would you like to see the risk measure and parameters, why?

<ESMA_QUESTION_PRIIPs_12>
We would not favour this approach. We believe that developing internal models will only be practical for larger manufacturers. It also requires regulators to invest a lot of time and cost to approve these. We believe that a standard model issued by the regulator is more transparent and creates a level playing field for all manufacturers. However we believe that the onus should be on manufacturers to show that the standard model is appropriate for their business and they should produce supplementary information to demonstrate the risks if necessary. <ESMA_QUESTION_PRIIPs_12>

13. Please state your views on the potential use of a two-level indicator. What kind of differentiators should be set both for the first level and the second level of such an indicator?

<ESMA_QUESTION_PRIIPs_13>
We disagree with this as it has the potential for confusion in understanding the risk. It also reduces comparability with the UCITS measures.
<ESMA_QUESTION_PRIIPs_13>

14. Do you have suggestions or concrete proposals on which risk scale to use and where or how the cut-off points should be determined?

<ESMA_QUESTION_PRIIPs_14>
These should be similar to the UCITS buckets.
<ESMA_QUESTION_PRIIPs_14>

15. Please express your views on the assessment described above and the relative relevance of the different criteria that may be considered.

<ESMA_QUESTION_PRIIPs_15>
We believe that a probabilistic approach using percentiles is the most appropriate
<ESMA_QUESTION_PRIIPs_15>

16. Do you think that these principles are sufficient to avoid the risks of manufacturers presenting a non-realistic performance picture of the product? Do you think that they should be reinforced?

<ESMA_QUESTION_PRIIPs_16>
We believe that manufacturers should use a prescribed model. In addition, if the manufacturer believes that the prescribed model is not appropriate, additional what if scenarios should be provided. The onus should be on the manufacturer to be prepared to defend why additional scenarios were not provided.
<ESMA_QUESTION_PRIIPs_16>

17. Do you think the options presented would represent appropriate performance scenarios? What other standardized scenarios may be fixed?

<ESMA_QUESTION_PRIIPs_17>
No we believe that manufacturers should determine the “what if” scenarios and be prepared to justify why they are appropriate.
<ESMA_QUESTION_PRIIPs_17>

18. Which percentiles do you think should be set?

<ESMA_QUESTION_PRIIPs_18>

25th/75th percentiles or 10th/90th percentiles. We believe using 3 percentiles (e.g. 50th) may lead the user to focus on the central one and place considerable weight on this as an expected outcome.
<ESMA_QUESTION_PRIIPs_18>

19. Do you have any views on possible combinations?

<ESMA_QUESTION_PRIIPs_19>
We believe that combinations should only be used where the prescribed model is not appropriate. The onus should be on the manufacture to use additional scenarios to demonstrate the risk.
<ESMA_QUESTION_PRIIPs_19>

20. Do you think that credit events should be considered in the performance scenarios?

<ESMA_QUESTION_PRIIPs_20>
Given the potential range of outcomes for credit events (illiquidity period, loss given default variations etc.), we believe that this should be disclosed as a risk but without showing scenarios.
<ESMA_QUESTION_PRIIPs_20>

21. Do you think that such redemption events should be considered in the performance scenarios?

<ESMA_QUESTION_PRIIPs_21>
Yes. These should be shown where the prescribed model does not demonstrate these adequately for products classified as complex.
<ESMA_QUESTION_PRIIPs_21>

22. Do you think that performance in the case of exit before the recommended holding period should be shown? Do you think that fair value should be the figure shown in the case of structured products, other bonds or AIFs? Do you see any other methodological issues in computing performance in several holding periods?

<ESMA_QUESTION_PRIIPs_22>
Yes.

Yes. The fair value should be the surrender value of the structured product (i.e. the value if it was resold to the manufacturer under the circumstances used in the projection.

We see no methodological issues.
<ESMA_QUESTION_PRIIPs_22>

23. Are the two types of entry costs listed here clear enough? Should the list be further detailed or completed (notably in the case of acquisition costs)? Should some of these costs included in the on-going charges?

<ESMA_QUESTION_PRIIPs_23>
We believe there should be explicit reference to exit costs or penalties. Entry/exit costs and on-going costs should be kept separate based on current proposed allocation.
<ESMA_QUESTION_PRIIPs_23>

24. How should the list be completed? Do you think this list should explicitly mention carried interest in the case of private equity funds?

<ESMA_QUESTION_PRIIPs_24>
Add distribution agent to investment adviser (to extent not already covered in earlier definitions or in (g) below).
Include carried interest either here or under (h) – Performance Fees
<ESMA_QUESTION_PRIIPs_24>

25. Should these fees be further specified?

<ESMA_QUESTION_PRIIPs_25>
No.
<ESMA_QUESTION_PRIIPs_25>

26. Should these fees be further specified? The "recovering fees" cover the following situation: when an investor receives income from foreign investments, the third-country government may heavily tax it. Investors may be entitled to reclaim the difference but they will still lose money in the recovering process (fee to be paid).

<ESMA_QUESTION_PRIIPs_26>
Licence fees should be added to the list.
<ESMA_QUESTION_PRIIPs_26>

27. Should these fees be further specified? The "recovering fees" cover the following situation: when an investor receives income from foreign investments, the third-country government may heavily tax it. Investors may be entitled to reclaim the difference but they will still lose money in the recovering process (fee to be paid).

<ESMA_QUESTION_PRIIPs_27>
No.
<ESMA_QUESTION_PRIIPs_27>

28. This list is taken from the CESR guidelines on cost disclosure for UCITS. What is missing in the case of retail AIFs (real estate funds, private equity funds)?

<ESMA_QUESTION_PRIIPs_28>
The net costs to the investor should be captured. We believe consistency with UCITS is paramount.
<ESMA_QUESTION_PRIIPs_28>

29. Which are the specific issues in relation to this type of costs?

<ESMA_QUESTION_PRIIPs_29>
How to determine appropriate rate of interest on borrowings? This should be consistent with future returns (x% over LIBOR) or if fixed, that rate should be used.
<ESMA_QUESTION_PRIIPs_29>

30. Is it relevant to include this type of costs in the costs to be disclosed in the on-going charges? Which are the specific issues in relation to this type of costs? Which definition of Costs for capital guarantee or capital protection would you suggest? (Contribution for deposit insurance or cost of external guarantor?)

<ESMA_QUESTION_PRIIPs_30>

i) Yes, these costs will reduce returns and so should be included.
ii) How to determine protection costs for an individual product or investment where the costs of protection is applied at an overall company level (e.g. deposit insurance)
iii) The cost of appropriate insurance or guarantee, or the cost of the financial instrument backing a capital guarantee or guaranteed return.
<ESMA_QUESTION_PRIIPs_30>

31. Which are the specific issues in relation to this type of costs? Should the scope of these costs be narrowed to administrative costs in connection with investments in derivative instruments? In that respect, it could be argued that margin calls itself should not be considered as costs. The possible rationale behind this reasoning would be that margin calls may result in missed revenues, since no return is realized on the cash amount that is deposited, and that:

<ESMA_QUESTION_PRIIPs_31>
The costs should be restricted to administrative payments, levies and moneys actually paid to another institution/government etc. when holding a financial instrument. Margin call should not be included in definition of costs for this purpose.
<ESMA_QUESTION_PRIIPs_31>

32. Which are the specific issues in relation to this type of costs? Should this type of costs be further detailed/ defined?

<ESMA_QUESTION_PRIIPs_32>
More detailed needed on "goods/services to be included".
<ESMA_QUESTION_PRIIPs_32>

33. How to deal with the uncertainty if, how and when the dividend will be paid out to the investors? Do you agree that dividends can be measured ex-post and estimated ex-ante and that estimation of future dividends for main indices are normally available?

<ESMA_QUESTION_PRIIPs_33>
Payment or non-payment of dividends to investors can be dealt with two ways:
i) Expected return includes capital growth and dividend elements. If dividend is not paid, a lower expected return is used.
ii) Always assume expected return includes both capital growth and dividends, and where dividends are not paid out, increase costs accordingly.
Our preferred approach is (i).
Dividends can be estimated in advance and indices are available for all major indices to help in estimating returns.
<ESMA_QUESTION_PRIIPs_33>

34. Is this description comprehensive?

<ESMA_QUESTION_PRIIPs_34>
Yes.
<ESMA_QUESTION_PRIIPs_34>

35. Can you identify any difficulties with calculating and presenting explicit broker commissions? How can explicit broker commissions best be calculated ex-ante?

<ESMA_QUESTION_PRIIPs_35>

Broker commissions will depend on the amount of trading within a fund and cannot be known in advance. Historic figures for portfolio turnover and the like are not a reliable guide to future costs, and will not exist for new PRIIPs in any event.
To calculate ex-ante, assumptions will be needed about portfolio turnover, broker commissions etc. and the regulations will need to specify such assumptions.
<ESMA_QUESTION_PRIIPs_35>

36. How can the total of costs related to transaction taxes best be calculated? How should this be done to give the best estimate ex-ante? Are there other explicit costs relating to transactions that should be identified? Do you think that ticket fees (booking fees paid to custody banks that are billed separately from the annual custodian fee paid for depositing the securities) should be added to this list?

<ESMA_QUESTION_PRIIPs_36>
Similar approach to Q35. We believe estimates should be required.
<ESMA_QUESTION_PRIIPs_36>

37. As regards the abovementioned estimate, can the fair value approach be used?[2]

<ESMA_QUESTION_PRIIPs_37>
We believe that the approach should be consistent with UCITS.
<ESMA_QUESTION_PRIIPs_37>

38. Can you identify any other difficulties with calculating and presenting the bid-ask spread? Do you believe broker commissions included in the spread should be disclosed? If so, which of the above mentioned approaches do you think would be more suitable for ex-ante calculations or are there alternative methods not explored above?

<ESMA_QUESTION_PRIIPs_38>
Broker commissions should not be separately disclosed but included as part of the overall disclosure (see approach at start at 3rd paragraph on page 61).
<ESMA_QUESTION_PRIIPs_38>

39. Do you believe that market impact costs should be part of the costs presented under the PRIIPs regulation? If so, how can the market impact costs best be calculated? How should this be done to give the best estimate ex-ante?

<ESMA_QUESTION_PRIIPs_39>
No. This is too difficult to quantify or predict accurately.
<ESMA_QUESTION_PRIIPs_39>

40. How should entry- and exit charges be calculated considering the different ways of charging these charges? How should this be done to give the best estimate ex-ante? Can you identify any other problems related to calculating and presenting entry- and exit fees?

<ESMA_QUESTION_PRIIPs_40>

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[2] One could also argue that all fund managers either have their own dealing desk or sub-contract this to other dealing desks. Since the principle of Best Execution is paramount, the dealers should know the typical spread in the securities with which they deal.

For funds that use dual pricing or a dilution levy, the expected amount of the bid/ask spread or levy will be known ex-ante and should be used to determine charges.
Swing pricing may or may not apply depending on cash flows at time of entry/exit and so cannot be known ex-ante. Prescribed assumptions as to application of swing pricing should be considered.
<ESMA_QUESTION_PRIIPs_40>

41. Which other technical specifications would you suggest adding to the abovementioned methodology? Which other technical issues do you identify as regards the implementation of the methodology?

<ESMA_QUESTION_PRIIPs_41>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_PRIIPs_41>

42. Do you think that an explicit definition of performance fees should be included? Do you think the definition by IOSCO is relevant in the specific context of the cost disclosure of the PRIIPs Regulation?

<ESMA_QUESTION_PRIIPs_42>
Yes and the IOSCO definition is a good starting point.
<ESMA_QUESTION_PRIIPs_42>

43. What would be the appropriate assumption for the rate of returns, in general and in the specific case of the calculation of performance fees?

<ESMA_QUESTION_PRIIPs_43>
Technical guidance is needed on the appropriate rate of return assumptions for different asset classes. This will also need to include the likely distribution of returns, say for the 10th and 90th percentiles. There are existing studies showing historic or projected returns for asset classes that can be used as a starting point.
The Technical Guidance should also include assumptions as to the appropriate “out-performance” assumptions to use for various asset categories to assure consistency in the application of performance fees across different PRIIPs.
<ESMA_QUESTION_PRIIPs_43>

44. Which option do you favor? Do you identify another possible approach to the disclosure and calculation of performance fees in the context of the KID?

<ESMA_QUESTION_PRIIPs_44>
Option 2 should not be used. The payment or not of performance fees in the past is no indication of the likely occurrence of performance fees in the future, and may lead to inaccurate information being provided.
Option 1 is the preferred scenario.
<ESMA_QUESTION_PRIIPs_44>

45. Which of the above mentioned options 1 and 2 for the calculation of aggregate costs would you prefer? Do you agree with above mentioned assumptions on the specificities of the costs of life-insurance products? How should the breakdown of costs showing costs specific to the insurance cover be specified? Do you think that risk-type riders (e.g. term or disability or accident insurances) have to be disregarded in the calculation of the aggregated cost indicator? How shall risk-type rider be defined

in this context? (one possible approach might be: A risk-type rider in this context is an additional insurance cover without a savings element, which has separate contractual terms and separate premiums and that the customer is not obliged to buy as a compulsory part of the product).

<ESMA_QUESTION_PRIIPs_45>
We believe that Option 2 would be appropriate with the proviso that the costs are separated out. For example, in the case of RIY, the total RIY is [x]% of which the biometric component is [y]% and the cost of guarantees is [z]%.
<ESMA_QUESTION_PRIIPs_45>

46. Do you think this list is comprehensive? Should these different types of costs be further defined?

<ESMA_QUESTION_PRIIPs_46>
We believe the costs and definitions should be consistent with UCITS.
<ESMA_QUESTION_PRIIPs_46>

47. Do you agree that guaranteed interest rate and surrender options should be handled in the above mentioned way? Do you know other contractual options, which have to be considered? If yes how?

<ESMA_QUESTION_PRIIPs_47>
Broadly we agree. Any implicit guarantees that are borne by a fund should be valued as if they were on a stand alone basis. This may be achieved through the calculation of the cost of the guarantee or an assumed change in investments over the life of the policy (with a lower growth rate) to meet the guarantee. Guaranteed annuity options also need to be considered.
<ESMA_QUESTION_PRIIPs_47>

48. Should the methodology for the calculation of these costs be further specified?

<ESMA_QUESTION_PRIIPs_48>
Yes. We would suggest that market consistency is paramount. There are well established processes for using market consistent models.
<ESMA_QUESTION_PRIIPs_48>

49. Do you think this list and breakdown is comprehensive?

<ESMA_QUESTION_PRIIPs_49>
Yes. This should be as consistent as possible with the definitions of UCITS. For underlying fund reallocations, this should be excluded unless the fund reallocation is required by the contract (i.e. moving to guaranteed funds closer to retirement).
<ESMA_QUESTION_PRIIPs_49>

50. Should the methodology for the calculation of these costs be further specified? How?

<ESMA_QUESTION_PRIIPs_50>
See answer to Q49.
<ESMA_QUESTION_PRIIPs_50>

51. Should the methodology for the calculation of these costs be further specified? How?

<ESMA_QUESTION_PRIIPs_51>
These are typically included in any administration costs charged to the policyholders.
<ESMA_QUESTION_PRIIPs_51>

52. Should the methodology for the calculation of these costs be further specified?

<ESMA_QUESTION_PRIIPs_52>
These should be consistent with UCITS. The projection of the surrender value on a year by year basis (as suggested earlier) is a good way of showing all the aggregate costs.
<ESMA_QUESTION_PRIIPs_52>

53. Should the methodology for the calculation of these costs be further specified? How? Do fund related costs also exist for with profit life insurance products?

<ESMA_QUESTION_PRIIPs_53>
These should be consistent with UCITS. In certain jurisdictions with profits funds have to disclose their costs. The current costs should be used any projections.
<ESMA_QUESTION_PRIIPs_53>

54. How to ensure that the look-through approach is consistent with what is applied in the case of funds of funds?

<ESMA_QUESTION_PRIIPs_54>
We believe that this should be consistent with process used for UCITS.
<ESMA_QUESTION_PRIIPs_54>

55. Should the methodology for the calculation of these costs be further specified?

<ESMA_QUESTION_PRIIPs_55>
See answer to Q54.
<ESMA_QUESTION_PRIIPs_55>

56. Which above mentioned or further options do you support, and why? More generally, how to measure costs that are passed to policy holders via profit participation mechanisms? Would you say that they are known to the insurance company? Do you think an estimate based on the previous historical data is the most appropriate methodology for the calculation of these costs?

<ESMA_QUESTION_PRIIPs_56>
We believe that all the costs should be projected. Where there is profit sharing this should appear as a reduction in costs based on the expected profit sharing on the basis of the projection assumptions. We do not believe historical profit sharing is appropriate.
<ESMA_QUESTION_PRIIPs_56>

57. Is this type of costs really specific to with-profit life-insurance products? Do you agree that these costs should be accounted for as on-going costs?

<ESMA_QUESTION_PRIIPs_57>
No. We believe they should be disclosed.
<ESMA_QUESTION_PRIIPs_57>

58. Do you think the list of costs of life-insurance products presented above is comprehensive? Which types of costs should be added?

<ESMA_QUESTION_PRIIPs_58>
Yes. It is comprehensive.
<ESMA_QUESTION_PRIIPs_58>

59. To what extent are those two approaches similar and should lead to the same results?

<ESMA_QUESTION_PRIIPs_59>
We believe the intrinsic value of fair value option is the best option. The first option opens the possibility for 'hiding' charges in the price of the hedging assets especially if transacted through an associated company as is commonly the case.

The fair value can often be determined as the cost of purchasing a hedging portfolio of bonds and traded options. Where this is not the case the use of a model may be permitted with regulation limiting the scope of model calibration and selection to prevent 'gaming' of the system by product manufacturers.
<ESMA_QUESTION_PRIIPs_59>

60. In comparison to structured products, do you see any specificity of costs of structured deposits? Do you think that the potential external guarantees of structured deposits might just have to be taken into account in the estimation of the fair value of these products?

<ESMA_QUESTION_PRIIPs_60>
No – a similar approach to that for structured products should be used. If there is an external guarantee for which the investor is not directly paying for then it should not be included in the costs.
<ESMA_QUESTION_PRIIPs_60>

61. Do you agree with the above mentioned list of entry costs? Which of these costs are embedded in the price? Should we differentiate between "delta 1" and "option based" structured products? In which cases do you think that some of these costs might not be known to the manufacturer? Which of these types of costs should be further defined?

<ESMA_QUESTION_PRIIPs_61>
Yes. We believe that for most structured products all the above costs are embedded in the price other than for some explicit 'courtage' fees applying to some products.
<ESMA_QUESTION_PRIIPs_61>

62. To what extent do you think these types of costs should be further defined and detailed?

<ESMA_QUESTION_PRIIPs_62>
The ESA's should as far as possible enumerate the different types of costs to be included but also add a principle that all expenses or charges or other costs borne by the investor not specifically mentioned in the regulations should be included and that those costs are calculated on an 'arm's length basis'.
<ESMA_QUESTION_PRIIPs_62>

63. How would you estimate ex ante the spread referred to above in (b), in the case the product is listed as in the case it is not? Should maximum spreads, when available, be

considered? Should the term "proportional fees" be further defined? Which definition would you suggest?

<ESMA_QUESTION_PRIIPs_63>
Assuming the repurchase of a product represents an early exit then the maximum spread should be disclosed in the early redemption section of the KID.
<ESMA_QUESTION_PRIIPs_63>

64. Do you agree with the list of costs outlined above? Which types of costs would require more precise definitions? To what extent should the methodology be prescriptive in the definition and calculation methodologies of the different types of costs?

<ESMA_QUESTION_PRIIPs_64>
Yes.
<ESMA_QUESTION_PRIIPs_64>

65. Would you include other cost components?

<ESMA_QUESTION_PRIIPs_65>
No.
<ESMA_QUESTION_PRIIPs_65>

66. Under which hypothesis should the costs of the underlying be included?

<ESMA_QUESTION_PRIIPs_66>
They should be based on current market conditions.
<ESMA_QUESTION_PRIIPs_66>

67. How would you deal with the issue of the amortization of the entry costs during the life of the product? For derivatives it will be notably important to define what the invested capital is, in order to calculate percentages. The possibilities include: the amount paid (i.e. option premium price or initial margin/collateral) or the exposure (to be defined for optional derivatives). Do you see other possible approaches on this specific point?

<ESMA_QUESTION_PRIIPs_67>
We believe RIY is the best indicator of total costs. Therefore entry costs would be included as a day 1 expense in the calculation of the net return.
<ESMA_QUESTION_PRIIPs_67>

68. Do you think that there are products with ongoing hedging costs (to ensure that the manufacturer is able to replicate the performance of the derivative component of the structured product)?

<ESMA_QUESTION_PRIIPs_68>
Yes.
<ESMA_QUESTION_PRIIPs_68>

69. Do you agree with the general framework outlined above?

<ESMA_QUESTION_PRIIPs_69>

Yes.
<ESMA_QUESTION_PRIIPs_69>

70. Which criteria should be chosen to update the values in the KID when input data change significantly?

<ESMA_QUESTION_PRIIPs_70>
The KID should be updated if, as a result of input data changes, the total cost indicator changes by a material amount. The ESA's should determine what a material amount is for this purpose but we suggest 15% change in the calculated cost before requiring a change to the KID.
<ESMA_QUESTION_PRIIPs_70>

71. As the evolution of underlying asset/s should be taken into account, are there specific issues to be tackled with in relation to specific types of underlying? To what extent should the RTS be prescriptive on the risk premium?

<ESMA_QUESTION_PRIIPs_71>
We believe that credit event linked derivatives when used in structured products present challenges for projecting the performance scenarios. We suggest that products incorporating such features are classified as complex products.

We believe the risk premium should be specified by broad asset class.
<ESMA_QUESTION_PRIIPs_71>

72. Are you aware of any other assumptions to be set?

<ESMA_QUESTION_PRIIPs_72>
No.
<ESMA_QUESTION_PRIIPs_72>

73. Having in mind that most of the applied models in banking are forward looking (e.g. using implied volatility instead of historical volatility) which are the pros and cons of backward looking approach and forward looking approach?

<ESMA_QUESTION_PRIIPs_73>
We prefer a forward looking approach as we believe this is less sensitive to changes in historical conditions and also better reflects what the costs to the issuer will be in reality.
<ESMA_QUESTION_PRIIPs_73>

74. Do you think that there are other risk free curves that could be considered?

<ESMA_QUESTION_PRIIPs_74>
No.
<ESMA_QUESTION_PRIIPs_74>

75. Do you think that there are other market data that could be used to determine the credit risk? Do you think that implied credit spreads from other issuer bonds (other than structured products) could be used?

<ESMA_QUESTION_PRIIPs_75>
We are not aware of other data.
<ESMA_QUESTION_PRIIPs_75>

76. How would you determine the credit risk in the absence of market data and which are the criteria to identify the comparable?

<ESMA_QUESTION_PRIIPs_76>
We believe that credit risk should be reflected in the risk section of the KID and as such excluded from the performance scenarios.
<ESMA_QUESTION_PRIIPs_76>

77. How would you include the counterparty risk in the valuation? Would you include specific models to include counterparty risk in valuation (CVA models)? How would you consider the counterparty risk for pure derivatives?

<ESMA_QUESTION_PRIIPs_77>
Counterparty risk should be reflected in the risk indicator by means of a narrative description. As such it does not then need to also be included in the costs.
<ESMA_QUESTION_PRIIPs_77>

78. In which circumstances do you think parameters cannot be computed/estimated using market data? What would you suggest to deal with this issue?

<ESMA_QUESTION_PRIIPs_78>
We believe a mark to model approach would be appropriate. The process has been broadly described on page 91 of the Paper.
<ESMA_QUESTION_PRIIPs_78>

79. Would it be meaningful to prescribe specific pricing models for structured products, derivatives and CFDs? If yes which are the pros and cons of parametric and non-parametric models?

<ESMA_QUESTION_PRIIPs_79>
It may be useful to prescribe pricing models for certain types of 'vanilla' structured products where such models can be comparable and relatively simple. This could be done in conjunction with the definition of 'complex' products foreseen by the PRIIPs regulation such that when a product is deemed complex it can also then deviate from standard pricing models to the use of the Firm's own model within the described governance framework.
<ESMA_QUESTION_PRIIPs_79>

80. What should be the value of x? (in the case of UCITS, x=5, but the extent to which this is appropriate for other types of PRIIPs, notably life-insurance products, is unclear).

<ESMA_QUESTION_PRIIPs_80>
We believe that we should maintain consistency with UCITS and KIIDs i.e. x = 5.
<ESMA_QUESTION_PRIIPs_80>

81. Should this principle be further explained / detailed? Should the terms "rank pari passu" be adapted to fit the different types of PRIIPs?

<ESMA_QUESTION_PRIIPs_81>
The principle should be expanded to include not just each share class, but each type of product or any other way similar PRIIPs are marketed, distributed or determined. Share class is a term related to UCITS-

type products but not all PRIIPs may have or use the term “share class”, instead using “series”, “version” etc.
<ESMA_QUESTION_PRIIPs_81>

82. What should be the relevant figure for the initial invested amount to be taken into account for the calculation of cost figures? Should a higher initial investment amount be taken into account not to overestimate the impact of fixed costs? How should the situation of products with regular payments be taken into account for that specific purpose? (Would an invested amount of 1 000 euros per period of time be a relevant figure?)

<ESMA_QUESTION_PRIIPs_82>
We believe that the minimum premium acceptable under the product should be used. Manufacturers could also be given the opportunity to show an additional higher figure for initial investment.
<ESMA_QUESTION_PRIIPs_82>

83. For some life-insurance products, the costs will differ on the age of the customer and other parameters. How to take into account this specific type of PRIIPs for the purpose of aggregating the costs? Should several KIDs for several ages be considered?

<ESMA_QUESTION_PRIIPs_83>
Generic pre-sale KIDs for more should be considered. A specific age related document could be provided on sale.
<ESMA_QUESTION_PRIIPs_83>

84. Do you agree with the abovementioned considerations? Which difficulties do you identify in the annualisation of costs?

<ESMA_QUESTION_PRIIPs_84>
We believe that if this measure is used it should be consistent with UCITS. We would favour the use of reduction in yield.
<ESMA_QUESTION_PRIIPs_84>

85. Which other assumptions would be needed there? In the case of life-insurance products, to what extent should the amortization methodology related to the amortization methodology of the premium calculation? To what extent should the chosen holding period be related to the recommended holding period?

<ESMA_QUESTION_PRIIPs_85>
We favour the reduction in yield measure which we believe is far more appropriate.
<ESMA_QUESTION_PRIIPs_85>

86. This definition of the ratio is taken from the CESR guidelines on cost disclosure for UCITS. Is it appropriate also in the case of retail AIFs? Should it be amended? Another approach to calculate these costs is to calculate the ratio of the total of these amortized costs to the invested amount in the fund. However in that case the question remains as to how to aggregate this ratio with the on-going charges ratio. Another possible approach could be to use the ratio between the total amount of costs over the

holding period and the average net investment (assumed during the whole period, in order to take into account future additional investments, partial withdrawals, payments (i.e. programmed investments or disinvestments)). Do you think this approach would be appropriate?**

<ESMA_QUESTION_PRIIPs_86>
Consistency with UCITS is preferred approach where possible. Average net assets should be used to take account of expected investment returns.
<ESMA_QUESTION_PRIIPs_86>

87. What would be other options to define the TCR ratio in the case of life-insurance products? What about the case of regular payments or regular increasing? Which definition would you favour? How to ensure a level playing field and a common definition with the other types of PRIIPs in this regard? Another possible approach could be to use the ratio between the total amount of costs over the holding period and the average net investment (assumed during the whole period, in order to take into account future additional investments, partial withdrawals, payments (i.e. programmed investments or disinvestments)). Do you think this approach would be appropriate? To what extent do these possible calculation methodologies fit the case of insurance products with regular payments?

<ESMA_QUESTION_PRIIPs_87>
We favour a reduction in yield approach as it captures all the issues described above.
<ESMA_QUESTION_PRIIPs_87>

88. What would be other options to define the TCR ratio in the case of structured products? Do you identify other specific issues in relation to the TCR if applied to structured products? Another possible approach could be to use the ratio between the total amount of costs over the holding period and the average net investment (assumed during the whole period, in order to take into account future additional investments, partial withdrawals, payments (i.e. programmed investments or disinvestments)). Do you think this approach would be appropriate? For derivatives, it might be the case that it is necessary to further define the concept of investment to be used as denominator of the ratio. Possibilities include the use of the actual sums paid and received (i.e. initial margins, variation margins, collateral postings, various payoffs, etc.) or the use of the exposure (i.e. market value of the derivative underlying). Do you think these approaches would be appropriate?

<ESMA_QUESTION_PRIIPs_88>
See answer to Q87
<ESMA_QUESTION_PRIIPs_88>

89. This definition of the ratio is taken from the CESR guidelines on cost disclosure for UCITS. Is it appropriate also in the case of retail AIFs? Should it be amended? Another possible approach could be to use the ratio between the total amount of costs over the holding period and the average net investment (assumed during the whole period,

in order to take into account future additional investments, partial withdrawals, payments (i.e. programmed investments or disinvestments)). Do you think this approach would be appropriate?

<ESMA_QUESTION_PRIIPs_89>
We believe that the definition should be consistent with that used for UCITS.
<ESMA_QUESTION_PRIIPs_89>

90. These different aforementioned principles are taken from the CESR guidelines on cost disclosure for UCITS. Is it also appropriate in the PRIIPs context?

<ESMA_QUESTION_PRIIPs_90>
Yes.
<ESMA_QUESTION_PRIIPs_90>

91. To what extent do the principles and methodologies presented for funds in the case of on-going charges apply to life-insurance products?

<ESMA_QUESTION_PRIIPs_91>
We believe that the reduction in yield approach is appropriate for life insurance products.
<ESMA_QUESTION_PRIIPs_91>

***92.* Do you think this methodology should be further detailed? To what extent do you think this methodology is appropriate and feasible (notably in terms of calibration of the model)? It might indeed be considered that valuation models for Solvency II usually are not likely to be designed for per contract calculations. Life insurers may restrict the calculation of technical provisions in the Solvency II-Balance-Sheet to homogenous risk groups. Furthermore they are allowed to use simplified calculation methods if the error is immaterial at the portfolio level. As profit sharing mechanisms in many countries are applied on the company level and not on a per contract level, projected cash flows from future discretionary benefits will not easily be broken down on a per product or even a per contract basis with the existing Solvency II-Valuation-Models.**

<ESMA_QUESTION_PRIIPs_92>
This is a good suggestion. We would envisage that Solvency II models would be an appropriate place to start and could be adapted to individual contracts. In addition, there is a governance process around the use of these models. There would need to be consistency with the process used for financial options (structured products etc.)
<ESMA_QUESTION_PRIIPs_92>

93. Do you identify any specific issue in relation to the implementation of the RIY approach to funds?

<ESMA_QUESTION_PRIIPs_93>
No.
<ESMA_QUESTION_PRIIPs_93>

94. In addition to the abovementioned issues and the issues raised in relation to TCR when applied to structured products, do you identify any other specific issue in relation to the implementation of the RIY approach to structured products?

<ESMA_QUESTION_PRIIPs_94>
No. Once the costs are identified they can easily be built into the RIY approach. The identification of cost is the issue and has been discussed earlier in the Paper
<ESMA_QUESTION_PRIIPs_94>

95. Do you agree with the above-mentioned assessment? Should the calculation basis for returns be the net investment amount (i.e. costs deducted)? Do you identify specific issues in relation to the calculation per se of the cumulative effect of costs?

<ESMA_QUESTION_PRIIPs_95>
Yes. Net figure should be used for return calculation returns.
<ESMA_QUESTION_PRIIPs_95>

96. Is this the structure of a typical transaction? What costs impact the return available to purchasers of the product?

<ESMA_QUESTION_PRIIPs_96>
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97. What costs impact the return paid on the products?

<ESMA_QUESTION_PRIIPs_97>
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98. What are the potential difficulties in calculating costs of an SPV investment using a TCR approach?

<ESMA_QUESTION_PRIIPs_98>
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99. What are the potential difficulties in calculating costs of an SPV investment using a RIY approach?

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