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Link to paper: https://www.esma.europa.eu/sites/default/files/library/jc-2019-63_consultation_paper_amendments_priips_kid.pdf

BETTER FINANCE Response

Executive Summary

General approach and review

As mandated by EU Law, the review process should have started with the Level 1 legislation in order to address key issues in the design of the PRIIPs KID; it would have offered the opportunity for proper consumer testing, focusing on risks, performance, and cost methodologies.

The PRIIPs Regulation still requires the European Commission to review it by 31 December 2019, while this Level 2 review is expected to be finalised in the second quarter of 2020.

This public consultation still constitutes a “quick fix” and will not be sufficient to effectively address all the issues that cause consumer detriment in the current disclosure document for PRIIPs. However, several of the fixes proposed by the ESAs would benefit individual savers and investors.

Future performance review

Future results cannot be accurately predicted, irrespective of the method applied. However, the new approach brings several advantages – such as better capturing the actual performance between the favourable and unfavourable scenarios – but estimates the returns of the underlying portfolio, and not of the PRIIP. Moreover, it generalises across PRIIPs, requires supplementary explanations and reduces comparability.

BETTER FINANCE proposes to replace the stochastic model of estimating returns with illustrative scenarios, where it would be shortly explained to the individual saver what could happen with the investment at a certain period of time and under certain market conditions (favourable, unfavourable, moderate).

Inclusion of past performance

Past performance is a pivotal element for making an informed investment decision. While past performance is not a reliable indicator of future results, it does show whether the asset manager achieved its stated investment objectives in the past. Past performance of the product (when available) should be presented in comparison with that of the capital market benchmark chosen by its manager on at least 10 years periods (or maximum available time span, if the product is younger).

Costs presentation

The future Reduction-in-Yield (RiY) is not a meaningful indicator of costs and causes confusion even for professional/ knowledgeable investors. Moreover, there is no standardised point in time on which the RiY is calculated in order to enable comparability.

The costs section of the PRIIPs must be simplified and allow comparison with other products. Presentation of costs both in percentage (%) and monetary figures (€/\$/£) is necessary to ensure investors understand the impact of fees and charges on their returns.

Costs for MOPs

Key Information Documents (KIDs) for Multi-Option Products (MOPs) must provide the total aggregate cost per investment option. It is not up to the individual investor to try to compute the total charges he has to pay. BETTER FINANCE proposes to the ESAs to require product manufacturers to distribute one individual KID per investment option, in accordance with Article 8 of the PRIIPs Regulation.

Contents

Table: Question classification by topic	3
Background information	3
1. General comment	4
2. Context and approach to review	10
3. PRIIPs Consumer Testing	12
4. Future performance scenarios	13
5. Inclusion of past performance	19
6. Methodology for calculation and presentation of cost information	21
7. UCITS exemption under PRIIPs	24
8. Provisions for Multi-Option Products (MOPs)	26

About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the public interest non-governmental organisation advocating and defending the interests of European citizens as financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances. It is the one and only European-level organisation solely dedicated to the representation of individual investors, savers and other financial services users.

BETTER FINANCE acts as an independent financial expertise and advocacy centre to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

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Instructions on how to read this paper: this document contains the response of BETTER FINANCE to the ESAs' JC Public Consultation but it is not the actual response form submitted.¹ Each section contains a **short summary** of the corresponding section in the Consultation Paper (CP) and of the questions analysed so the reader can understand the context. Each section aims to replicate the names and order of the CP's sections and topics.

The general comment below represents BETTER FINANCE's assessment of the entire Level 2 review process (incl. stakeholder consultations) conducted this year by the European Commission and the ESAs JC.

Table: Question classification by topic

SUBJECT	Question #	Topic/ Section
FUTURE PERFORMANCE	Questions 1-2	Digital solutions and machine-readable KIDs
	Questions 3-4	Implementation period for the new RTS (amendments)
	Question 5	General question
	Question 6	Consumer testing
	Questions 7 - 8	Removing intermediate and stress scenarios
	Questions 9 - 14	New methodological approach for future performance scenarios
COSTS PRESENTATION	Questions 15 - 17	Compensatory mechanisms
	Questions 18 - 20	Maximum Growth methodological approach (alternative)
	Questions 21 - 22	Other alternative methodologies
	Questions 23 - 25	Illustrative scenarios for structured products
	Questions 26 - 32	Inclusion of past performance in the PRIIPs KID
	Questions 33 - 42	Costs section (general)
	Question 43	Transaction Costs
	Question 44 - 49	Transposition measures for UCITS transition from the KIID to the KID
	Questions 50 - 54	Provisions for Multi-Option Products (MOPs) on costs
	Questions 55 - 57	Cost-benefit analysis

Background information

Manufacturers of retail investment products are required by EU law to produce a pre-contractual disclosure document explaining the *key characteristics* of financial products to retail investors, such as costs or risks. Currently, there are two such documents at EU level:

- **Key Investor Information Document** (KIID²) for investment funds (UCITS – Undertakings for Collective Investment in Transferable Securities³);

¹ The ESAs JC require to fill in a pre-formatted, standardised response form; we have chosen to change the format to make it more reader-friendly, to include background information and summaries for less knowledgeable readers and streamline comments, where possible.

² Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs) OJ L 352, 9.12.2014, p. 1–23, <http://data.europa.eu/eli/reg/2014/1286/oj>.

³ Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions OJ L 257, 28.8.2014, p. 186–213, <http://data.europa.eu/eli/dir/2014/91/oj>.

- Key Information Document (KID) for other PRIIPs (**P**ackaged **R**etail and **I**nsurance-based **I**ntestment **P**roducts⁴) such as life insurances, structured deposits, some types of bonds etc.

The UCITS are temporarily exempt from producing the PRIIPs KID until 31 December 2021;⁵ personal pension products, pillar I pensions, occupational pensions, IORPs and PEPPs are excluded from the scope of the PRIIPs KID.⁶

The European Commission is required to review the PRIIPs Level 1 Regulation by 31 December 2019. However, it mandated the ESAs to review and propose amendments to the Level 2 Regulation,⁷ process to which this public consultation is part of.

The current proposed amendments are aimed at the methodology to calculate and present performance scenarios and costs in the PRIIPs KID, at smoothing the transition for UCITS from the KIID to the KID,⁸ and targeted amendments for Multi-Option PRIIPs (MOP).

1. General comment

The Council of the EU, during the tenure of the Finnish Presidency, mentioned two significant objectives (and measures to be taken) in the *Conclusions for Deepening the Capital Markets Union*⁹ concerning consumers' need for transparency and disclosure:

- an assessment of the “current disclosure rules with a view to eliminating incoherent or incomprehensible information”; and
- the need to “ensure that information is clear, concise, understandable, proportionate and not - excessive or overlapping in quantity or content”.

This represents a clear initiative from the co-legislator to start the Level 1 PRIIPs Regulation review.

In these circumstances, we continue to be concerned by this review process as to:

- what type of information **is available** to be presented to non-professional, individual and small (“retail”) investors, and
- what retail investors **find useful** and **relevant** to make an informed investment decision.

⁴ Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs), OJ L352, 9.12.2014, p. 1–23, <http://data.europa.eu/eli/reg/2014/1286/oj>.

⁵ Article 32(1) PRIIPs Regulation.

⁶ Article 2(2) read in conjunction with Article 4(1) of the PRIIPs Regulation.

⁷ Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products (PRIIPs) by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents, C/2017/1473, OJ L 100, 12.4.2017, p. 1–52, http://data.europa.eu/eli/reg_del/2017/653/oj.

⁸ Page 6 of the [Consultation Paper](#).

⁹ Council Conclusions on the Deepening of the Capital Markets Union (5 December 2019), Brussels, 5 December 2019, (OR. en), 14815/19.

Chronology

The increased complexity and length of the UCITS prospectus lead to Directive 2001/107/EC¹⁰ requiring product manufacturers to publish a *simplified prospectus*, disclosing information on **actual (past) returns and costs**, in force as of 2005.¹¹

After a short period of implementation, the European Commission's 2006-2007 workshops on key investor information concluded that the simplified prospectus did not achieve its target¹² and a new document must be:

- unbundled from the Prospectus,
- **simplified**, streamlined,
- contain elements that are **actually useful** to retail investors, and
- take the **actual experience of retail investors** into account.

For this reason, the European Commission mandated an investor testing exercise in 2008 on the content and format of the Key Investor Information Document (KIID), which put forward strong conclusions:

- information overload and large blocks of text need to be avoided,
- consumers pay most attention to the risk-reward sections, and
- actual (past) performance is the information they expect to see in the KIID.

*The UCITS KIID is still today one of the most valuable sources of information for both retail investors and public authorities.*¹³

For reasons that BETTER FINANCE could not document,¹⁴ the PRIIPs regulation shifted from actual information (returns and costs) to estimations *in spite* of the PRIIPs Consumer Testing Exercise of 2015 mentioning among others that:

- “*respondents often wrongly assess likelihoods when shown performance scenarios*”;
- “*respondents made mistakes even when presented with information on probability*” of the estimated returns;
- “*respondents perform better when presented with simpler information*”, which in our view is a clear-cut actual (past) data;
- “*a minority of participants understood that the costs shown might not represent the actual costs they will pay*”; and
- “*most cost section's questions posed difficulties in understanding for participants*”,¹⁵

¹⁰ Directive 2001/107/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) with a view to regulating management companies and simplified prospectuses, OJ L 41, 13.2.2002, p. 20–34.

¹¹ Article 13c(9) read in conjunction with Schedule C of Directive 2001/107/EC.

¹² Talia B. Gillis, ‘Putting Disclosure to the Test: Towards Better Evidence-Based Policy’ (2015) 28(1) Loyola Consumer Law Review, 33-104, 59, available at <https://lawcommons.luc.edu/lclr/vol28/iss1/3>.

¹³ See BETTER FINANCE Assessment of the European Supervisory Authorities’ Reports on Costs and Performance of Retail Investment Products, <https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Assessment-ESAs-reports-FINAL-Feb-2019.pdf>.

¹⁴ BETTER FINANCE desk research did not find any document clearly spelling out that future performance is a better and more meaningful way to communicate the key performance data of a PRIIP.

¹⁵ European Commission, ‘Final Report: Consumer Testing Study of the Possible New Format and Content of for Retail Disclosures of Packaged Retail and Insurance-based Investment Products’ (2015) 18, hereinafter “PRIIPs CTE 2015” available https://ec.europa.eu/info/sites/info/files/consumer-testing-study-2015_en.pdf, emphasis added.

Moreover, the qualitative parts of the PRIIPs Consumer Testing exercise revealed that the factors causing most confusion for retail investors were:

- Understanding that the costs figures were not exact, and
- Understanding performance scenarios.¹⁶

Lastly, if additional explanations could be added to clarify issues for retail investors, research shows that information overload:

- reduces the attention and likelihood of investors to read the KID,¹⁷
- reduces their ability to understand the product,¹⁸ and
- reduces the “*perceived usefulness*” of the KID.¹⁹

Yet, the PRIIPs Regulation produced a longer, more complex, misleading and inaccurate key information document (KID), that by essence puts forward only estimations of future performances and future costs, and no actual or accurate financial data:

- in the risk and reward section:
 - i. probabilities of loss due to credit and market risk;
 - ii. probabilities of return factored in past performance data;
- in the costs section, estimations of future costs.

Ultimately, in order to address all these issues, the methodology proposed by the ESAs needs further explanations and caveats to inform non-professional investors of the limitations of information presented therein.

What must be weighted in when analysing the PRIIPs Consumer Testing exercise of 2015 is that:

- i. respondents and participants were presented with different versions of the same methodology, i.e. estimations of returns and costs; and that
- ii. **at no point in the past 20 years has consumer understanding of past performance been tested against understanding of return estimations.**

Contrary to its stated consultation work²⁰ and the trends of national competent authorities,²¹ the Proposal for a Regulation on PRIIPs²² in our view ignored evidence and reflected political ambition and financial industry preferences.

¹⁶ PRIIPs CTE 2015 (n 15) page 198.

¹⁷ European Commission, ‘Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council on Key Information Documents for Investment Products, COM(2012) 352 final, page 18, hereinafter “COM IA”, available here <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52012SC0187&from=EN>.

¹⁸ PRIIPs CTE 2015 (n 15) 219.

¹⁹ N. Gentile, N. Linciano, C. Lucarelli, P. Soccorso, ‘Financial Disclosure, Risk Perception and Investment Choice: Evidence from a Consumer Testing Exercise’ (2015) CONSOB, page 10, hereinafter “CONSOB CTE”, available at: <http://www.consob.it/documents/11973/204072/qdf82.pdf/58dc22f8-504b-4bad-9679-610306359dfc>.

²⁰ COM IA (n 17) 6-8.

²¹ Gentile, Linciano, Lucarelli, Soccorso (n 18) 16-19.

²² Proposal for a Regulation of the European Parliament and of the Council on key information documents for investment products, COM(2012) 352 final, 2012/0169 (COD).

It is still unimaginable why EU financial regulation warns that “past performance is not a reliable indicator of future results”²³ but at the same time obliges product manufacturers to estimate future results based exactly on past performance.²⁴

To this end, in BETTER FINANCE’s view it is less harmful to offer no information rather than misleading or confusing information to non-professional, individual and small investors. We also believe that public authorities and stakeholders must be reminded of the beneficiaries, functionality and purpose of a KID:

- **beneficiaries:** individual, non-professional and small investors and savers (“**retail**”);
- **functionality:** allow retail investors to *understand* and *compare* the PRIIP;
- **purpose:** allow retail investors to make *informed investment decisions*.

The debate on the review of the PRIIPs KID regulations has transformed in a “political crusade”, with different groups of stakeholders pulling in opposite directions. However, the PRIIPs KID must cater the needs and understanding of non-professional investors, not those of financial services providers.

Therefore, BETTER FINANCE believes that this public consultation is neither timely, nor efficient from a logical and a regulatory point of view. We are disappointed to see so much of the European Supervisory Authorities’ (ESAs) Joint Committee’s (JC) scarce and valuable resources for consumer protection²⁵ being misused in 2018-2019 for this PRIIPs Delegated Regulation (Level 2) review.

We wish to congratulate, however, the three ESAs on amassing efforts to put forward workable solutions at Level 2 in such a short period of time and on so many difficult and complex aspects, and we wish to manifest our intention, as we did previously, to collaborate and support the ESAs in reducing the detrimental nature of the PRIIPs KID. Nevertheless, BETTER FINANCE’s current input for the performance and cost methodologies does not represent an endorsement of the ideas put forward in the CP as such but is an attempt to provide an as-meaningful-as-possible document for EU retail investors, given the current regulatory situation.

The PRIIPs Regulation (Level 1) provided the deadline for the European Commission to conduct a full review on the application and implementation of the said legislative act before 31 December 2018, further delayed by legislative act²⁶ by 31 December 2019. Therefore, the public consultation of the ESAs JC in November 2018, the consumer testing exercise, the public hearing of November

²³ Article 44(6)(e) of the MiFID II DA (Commission Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive, L 87/) and the KIID Regulation (Commission Regulation (EU) No 583/2010 of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of a website OJ L 176, 10.7.2010, p. 1–15).

²⁴ Annex II, pt. 9, read in conjunction with pt. 4 of Annex IV of Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products (PRIIPs) by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents, OJ L 100/1.

²⁵ Articles 9 and 10 of the founding Regulations (Regulation (EU) 1093/2010 – EBA – Regulation (EU) 1094/2010 – EIOPA – and Regulation (EU) 1095/2010 – ESMA).

²⁶ Article 17(2) of Regulation (EU) 2019/1156 of the European Parliament and of the Council of 20 June 2019 on facilitating cross-border distribution of collective investment investment undertakings and amending Regulations (EU) No 345/2013, (EU) No 346/2013 and (EU) No 1286/2014, OJ L 188/55.

2019 and this present consultation should have focused on the provisions at PRIIPs Regulation (Level 1), which are key:

- to solve the vast majority of issues raised by stakeholders and
- to solve the issues which the ESAs are attempting to provide a solution to.

In BETTER FINANCE's experience so far, the majority of issues raised by us and other stakeholders cannot be "fixed" through amendments on the PRIIPs Delegated Regulation (Level 2) and must be answered or validated by the co-legislators before going into the implementing details.

It is all the more disappointing to read in the Consultation Paper (hereinafter **CP**), quoting the February 2019 Final report, that *"where the information collected and analysis conducted [...] would indicate that changes to the PRIIPs Level 1 Regulation may be needed [...] the ESAs will consider whether it is relevant [...] recommend such changes to the co-legislators"*, without ESAs mentioning the need to address the performance and cost scenarios issues.

What is more, even the German Federal Financial Supervisory Authority (BaFin) announced that it opposed this consultation in the ESAs decision-making bodies and it will not provide feedback, stating that

*"In order to improve the key information document for retail investors, BaFin believes that the revision of the PRIIPs Regulation itself is required. This would allow in particular to specify the scope of application and to adapt the content and formats for digital development."*²⁷

Therefore, we urge the ESAs JC to reconsider their position on the costs section (summary cost indicator and Reduction-in-Yield) and on the risk and reward section (performance scenarios), take stock of the valuable input received from retail investors during this entire period and propose the co-legislators a quickly and early review of the said Regulation.

Moreover, on the basis of Article 33(1) of the PRIIPs Regulation, the consumer testing exercise should have been much wider in scope, rather than testing only the presentation format of future performance scenarios, as it is currently done. BETTER FINANCE firmly disagrees with the European Commission's exclusion²⁸ of the three testing options proposed²⁹ by the ESAs JC and believes there was no valid basis to do so.

In addition, BETTER FINANCE firmly advises the ESAs JC to cooperate with the European Insurance and Occupational Pensions Authority (EIOPA) which is currently developing the RTS for the Pan-European Personal Pensions (PEPP),³⁰ among which the specific KID is discussed.

²⁷ Own translation, see BaFin Journal (November 2019), page 10, *emphasis added*

https://www.bafin.de/SharedDocs/Downloads/DE/BaFinJournal/2019/bj_1911.pdf;jsessionid=B4261720A6256D3DF312CFA6A739EFF4.1_cid290?_blob=publicationFile&v=4.

²⁸ Letter of DG FISMA of 19 July 2019 (FISMA C4 LP/mp(2019)5240023) to the Joint Committee of the ESAs explaining the choice of the options for the consumer testing exercise on PRIIPs, available here:

<https://eiopa.europa.eu/Publications/COM%20letter%20to%20ESAs%20on%20exclusion%20of%20some%20performance%20scenarios%20PRIIPs%20consumer%20testing.pdf>.

²⁹ Letter of the Joint Committee of the ESAs to the Director-General of DG FISMA of 23 May 2019 (JC 2019 46) proposing options for the consumer testing exercise on PRIIPs – available here:

https://eiopa.europa.eu/Publications/Standards/JC%202019%20046_PRIIPs_Letter%20on%20consumer%20testing_COM.pdf

- Annex of the Letter available here:

https://eiopa.europa.eu/Publications/Standards/Annex_PRIIPs_Performance_options_consumer_testing.pdf.

³⁰ Regulation (EU) 2019/1238 of the European Parliament and of the Council 20 June 2019 on a pan-European Personal Pension Product (PEPP), OJ L 198/1.

BETTER FINANCE, as a representative of individual and small investors, believes that the outcome of the PRIIPs KID and PEPP KID must be correlated and as similar as possible with the UCITS KID, which proved a success of EU financial regulation so far.

Gaining comprehensive overview of the current complex regulatory landscape for retail investors can be a daunting task. The various new regulations, e.g. MiFID II, PRIIPs, IDD, Solvency II, IORP II, and rules applicable to banking products (savings accounts, structured notes, etc.) led to inconsistent standards of disclosure which create confusion among investors and unnecessarily increase the workload for distributors and manufacturers and by that costs for investors. Moreover, there is oversupply of pre-contractual key disclosure documents that are being offered at national level for retail investors (for instance, the German market provides 10 different product information sheets),³¹ lacking standardisation and hindering comparability and thus adding to investor confusion.

The three KI(I)D(s) must not be viewed in isolation and the ESAs must consider the interests of retail investors:

- to have access to simple, comparable information on retail investment products;
- to be able to make informed decisions; and
- the information presented to be fair, clear, and not misleading.

Designing differently (and presenting different categories of information) these three KIDs will not only build against the aforementioned principles and further hinder the ultimate purpose of KIDs in terms of enabling comparisons for potential clients between investment products, but will also constitute an infringement of the ESAs legal obligation to promote simplicity for consumers.³²

However, we believe that the ESAs did not properly address the topics set out in this paper, in particular essential questions that underline the work to be carried out, such as what is “key” in key information and what is relevant and useful for retail investors? In our view, since these aspects are not prescribed in the PRIIPs Regulation, nor in the recitals preceding the provisions thereof, the ESAs must shed light and settle these issues, as they have done with the scope of application of the aforementioned regulation in what concerned bonds.³³ More comments are comprised in the *consumer testing* section.

³¹ Currently, there are 10 key information sheets (*produktinformationsblätter*) available on the German retail market.

³² Article 9(1) of the founding regulations (Regulation (EU) 1093/2010 – EBA – Regulation (EU) 1094/2010 - EIOPA - and Regulation (EU) 1095/2010 – ESMA).

³³ Joint ESA Supervisory Statement – Application of the Scope of the PRIIPs Regulation to Bonds, (24 October 2019) JC-2019-64, available here https://www.esma.europa.eu/sites/default/files/library/jc-2019-64_priips_kid_supervisory_statement_bonds.pdf.

2. Context and approach to review

Short summary: The European Commission requested the ESAs to conduct a targeted review of the PRIIPs Delegated Regulation (Level 2). In light of the extension of the UCITS exemption and of the deadline for the review of Level 1 Regulation, and considering the input received from stakeholders during the November 2018 consultation on PRIIPs, the ESAs decided to limit the scope of the review only to three topics: performance scenarios, costs, and changes for PRIIPs offering a range of investment options (MOPs). **Questions analysed:** 1-5.

Digital solutions and machine-readable KIDs

Question 1: Are there provisions in the PRIIPs Regulation or Delegated Regulation that hinder the use of digital solutions for the KID?

The scope of this proposal (or question) has not been defined by the ESAs, making it difficult to answer. If the question refers to *digital solutions* as in providing the KIDs on durable mediums, such as electronic versions of the document or on websites, it follows clearly from the reading of Article 14(2), read in conjunction with paragraphs (4) and (5), that it is possible. In addition, BETTER FINANCE sees also portable (mobile) applications as natural extensions of the provisions of letter c) of Article 14(2).

If the ESAs refer to *digital solutions* as means to customise the content, format or order of presentation of the key information of the PRIIP, such as:

- dropdown lists, tabs, windows, flip-images, videos, or other means of information layering; or
- electronic features allowing for information customisation (such as computer-generated information),

a strict reading of the PRIIPs Regulation (Level 1) leads to the conclusion that such solutions would be contrary to the wording of the aforementioned provisions.

First, in our view the purpose of allowing the provision of KIDs on durable medium (as it is the case also with the UCITS Directive) is limited to disseminating or making available the electronic format of the document, online or offline.

Second, while Articles 13 and 14 of the PRIIPs Regulation (read in light of Recital 27) allow the retail investor to choose whether to receive the KID in paperback (hard) or electronic format, including electronic versions of documents or through a website, Articles 6(2) and 8(1), second indent, clearly require the provision of the key information in a document-like sequence and format, where the content cannot be changed in any manner.

BETTER FINANCE sees an opportunity to further investigate whether customising the information in KIDs through digital solutions would improve the understanding and engagement of retail investors, in particular since it would allow to produce tailor-made documents for each person in particular. Provided that the information is fair, clear and not misleading, digital distribution of PRIIPs KIDs should then help consumers compare even better between the different PRIIPs offerings.

In addition, digital tools could contain “nudging” features with regards to the prominent warnings contained in the PRIIPs KID so that the saver’s attention is drawn onto to them and so that the saver does not easily oversee the essential information, such as the prominent warnings. Nevertheless, we deem it also important for the ESAs to use the already available behavioural insights and behavioural experiments undertaken by some of the competent authorities as to the effectiveness of warnings and their impact on financial services users.

However, as the situation stands currently, this would represent **a clear breach of EU law** and it should be addressed at Level 1.

Question 2. Do you agree that it would be helpful if KIDs were published in a form that would allow for the information to be readily extracted using an IT tool?

BETTER FINANCE firmly believes this would be helpful, for the following reasons:

- It would facilitate the iteration of the reports on costs and past performance of the ESAs;
- It would facilitate harmonised reporting by NCAs;
- It would reduce the costs of data aggregation and reporting, especially in the context of developing web-comparison tools and online databases.

Therefore, BETTER FINANCE strongly supports this initiative.

Transitional period for implementing new RTS (amendments)

Question 3. Do you think that the amendments proposed in the consultation paper should be implemented for existing PRIIPs as soon as possible before the end of 2021, or only at the beginning of 2022?

BETTER FINANCE advises the ESAs to reduce the transitional periods for implementing the new requirements and impose the implementation of the PRIIPs amendments as soon as possible in order to reduce the detriment currently caused by the KID to individual, non-professional and small investors.

Question 4. Do you think that a graduated approach should be considered, whereby some of the requirements would be applied in a first step, followed by a second step at the beginning of 2022?

There is no reason for which a step-by-step approach could be applied. Moreover, considering the difficulties and complexity of the current requirements and of the proposed amendments, a graduated approach could lead to conceptual conflicts in the provision of the KID.

In addition, graduated approaches would result in the provision of different KIDs to potential retail clients, which would add even more to the confusion created by the KID and make it even more difficult for retail investors to assess and compare investment products.

General question

Question 5. Are there material issues that are not addressed in this consultation paper that you think should be part of this review of the PRIIPs Delegated Regulation? If so, please explain the issue and how it should be addressed.

BETTER FINANCE believes that, in absence of regulatory restraints at Level 1, it is in the remit of competence of the ESAs to consider **standardising, streamlining or introducing clear requirements on the assessment and assignment of recommended holding periods (RHP)** for PRIIPs. The RHP is not only crucial for the suitability of the PRIIP itself, but it also anchors essential elements, such as performance and costs, and should have been reviewed by the ESAs during this public consultation.

Moreover, in the context of revising the probabilistic future return scenarios, the ESAs did not make any mention on **the minimal necessary historical track record that would need to be used to estimate performances**. Considering the conclusions put forward in the February 2019 Report, and analysing in conjunction with the new proposals of this consultation paper, it is not clear whether the old 5-year period will be used or not.

3. PRIIPs Consumer Testing

Short summary: The European Commission decided to undertake a targeted consumer testing exercise on the presentation of performance information in the PRIIPs KID, asking the ESAs to make proposals to this extent. The ESAs proposed 13 options to be tested, including the current actual presentation, for three types of PRIIPs: structured and non-structured products, and IBIPs. The European Commission rejected three of the options, claiming inconsistency with the PRIIPs Level 1 regulation.

Question 6. Do you have comments on the modifications to the presentation of future performance scenarios being considered? Should other factors or changes be considered?

The key information document is addressed to individual, non-professional and small investors, who have a limited understanding and/or knowledge of financial products. The KID's function is twofold: (i) to enable retail investors understand the PRIIP; (ii) to enable comparisons among different PRIIPs. The purpose of the KID is to enable retail investors:

- make an informed investment decision;
- reduce reliance on investment advice;
- restore trust in the financial services industry.

Therefore, the KID should cater the needs of retail investors.

A consumer testing exercise is the best mean to identify what retail investors understand in terms of content and format, how long and how much information can be presented and, **most** importantly, what information should be avoided due to its misleading nature.

The current consumer testing exercise performed by the European Commission (EC) missed on most of the abovementioned aspects, which are **pivotal** for the clarification and proper implementation of the PRIIPs KID. Focusing only on the presentation of *future performance scenarios* leaves informational gaps in consumer understanding regarding costs and risks.

The 2008 UCITS KIID testing and the 2015 PRIIPs KID testing tested opposed presentations of information in the KIDs. On one side, the UCITS KIID testing analysed how retail investors perceive past performance presentation (and actual costs and risk information), while the 2015 PRIIPs KID testing examined how retail investors respond to estimated information. The two methodologies have not been tested together. The EC should have first tested which of the two approaches are more understandable by retail investors, lead to less hyperbolised assumptions and enable and facilitate a proper understanding of the nature and characteristics of a PRIIP.

Clarifying this question would have tremendously simplified the review process.

However, BETTER FINANCE agreed with the initial options proposed by the ESAs since it also tested inclusion of past performance and of illustrative scenarios.

4. Future performance scenarios

Short summary: the ESAs have developed a new methodology to calculate and present future performance scenarios in the PRIIPs KID, still based on a stochastic model; the ESAs propose to add a “compensatory mechanism” to limit maximums and minimum return projections. In addition, this section asks whether other future performance approaches (illustrative scenarios) could be considered. **Questions analysed:** 7 – 25.

Removing intermediate and stress scenarios

Question 7. If intermediate scenarios are to be included, how should they be calculated for Category 3 PRIIPs (e.g. structured products)? If intermediate scenarios are not shown in the performance section, which performance assumption should be used for the ‘What are the costs?’ section?

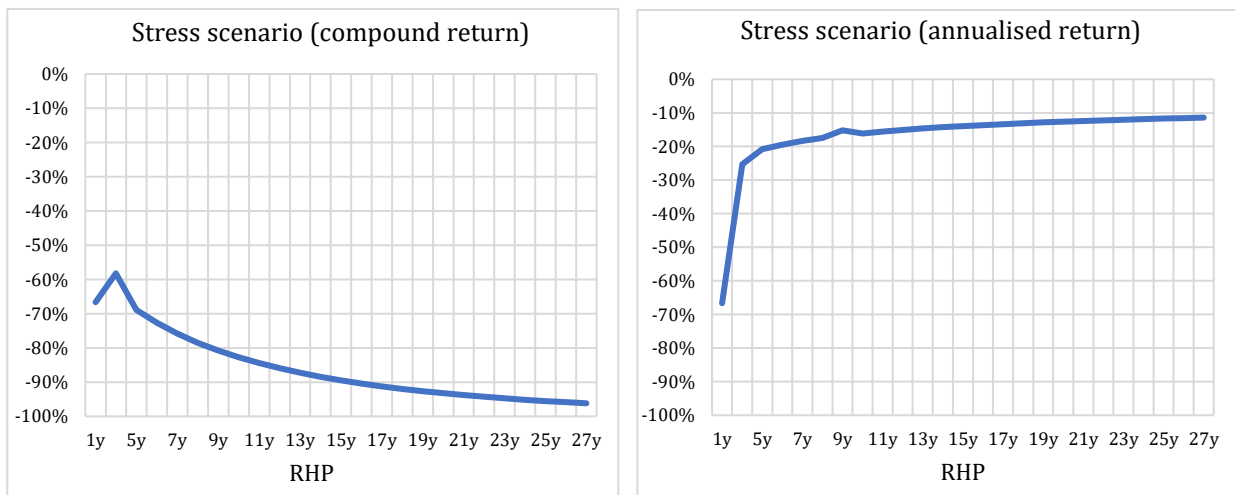
Since the Recommended Holding Period (RHP) is not standardised, the costs and performances may be incomparable at the maturity of the product. For this reason, the intermediate scenario (understood as half of the RHP) may also be incomparable between similar products. As such, if the intermediate scenario would be kept in the KID, it should be at a standardised point in time (for example, in 3 years), depending on the product based on three categories:

- for short-term products (RHP < 1 year), there should be no intermediate scenario;
- for medium-term products (3y < RHP ≤ 6y), the intermediate point should be set at 1 year;
- for products with 7y < RHP < 10Y, the intermediate point should be set at 4 years;
- for long-term products (RHP > 10y), the intermediate point should be set at 10 years.

For reasons of transparency, if the intermediate scenarios would not be disclosed at all in the KID, the summary cost indicator should not disclose costs at the reduction-in-yield (RiY) at that point. However, intermediate scenarios must be kept if quantified future performance disclosures are maintained (not the position of BETTER FINANCE). Otherwise, the disclosures would show only linear future performances through time, which is most of the time extremely misleading.

Question 8. If a stress scenario is included in the presentation of future performance scenarios, should the methodology be modified? If so, how?

The current methodology for the stress scenarios generates very confusing results for the retail investor: on one side, the cumulative performance constantly decreases (and tends to 0) as time passes by, but the annualised performance (return per year) increases as time passes by, as shown in the graphs below:



Source: BETTER FINANCE own calculations

Therefore, the stress scenario methodology should either be revised or replaced by a short and concise narrative explanation/ warning:

“Under a stress scenario (adverse market conditions, crises, political intervention), you could lose a significant part or even all your investment”.

New methodological approach for future performance scenarios

Question 9. Do you agree with how the reference rate is specified? If not, how should it be specified?

We agree that the reference rate should be country specific and read from the historical prices of sovereign bonds of the domicile, with two elements of circumstantiation:

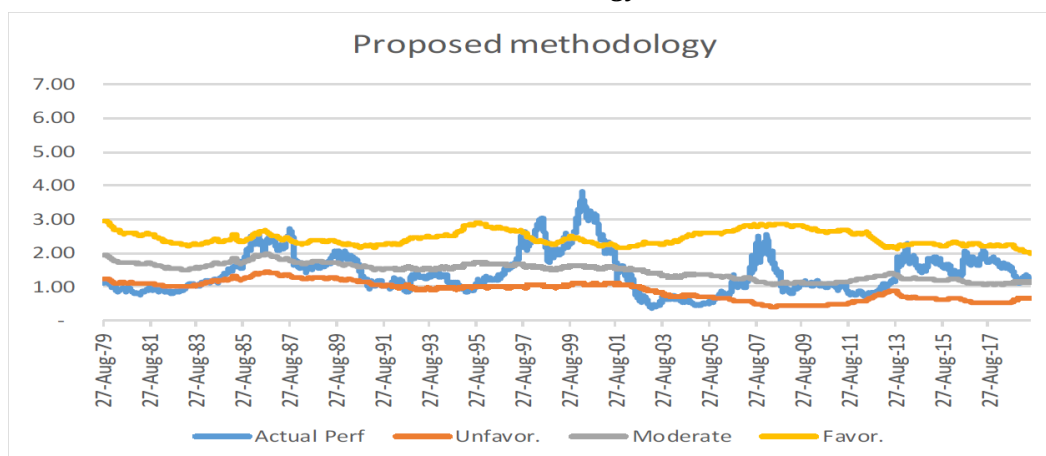
- for securities, the risk-free rate should be estimated only from the investment grade (AAA – C) bonds, thus eliminating the risky (speculative) ones; otherwise, there would be an additional risk premium included in the historical price of the fixed instrument;
- for indices, the risk-free rate (for EUR-denominated) should be based on the yield curve published by the European Central Bank for AAA-rated bonds.³⁴

If the securities’ class is cross-border (more than one domicile, as is for European small-caps), then the required rate of return should be either read from the securities’ index (ESAs could provide guidelines on it) or could be the weighted average of the risk-free rates of all domiciles involved plus the risk premia of the securities in all domiciles involved, in order to capture the weighted average of the domiciles’ risk.

Question 10. The revised methodology specifies that the risk premium is determined by future expected yields. The methodology further specifies that future expected yields should be determined by the composition of the PRIIP decomposed by asset class, country and sector or rating. Do you agree with this approach? If not, what approach would you favour?

Compared to the previous methodological approach for estimating future returns, the new approach brings improvements in terms of expectations for the saver as it manages to narrow down, on the majority of occasions, the minimum and maximum returns of the PRIIP within the favourable and moderate scenario, as shown in the graphs below:

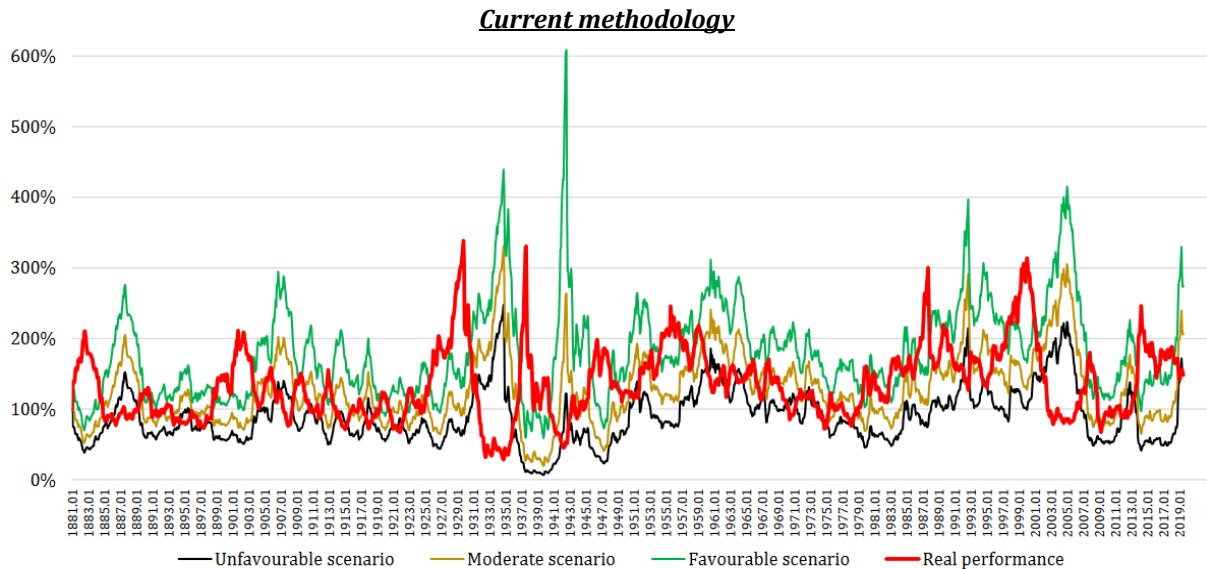
New methodology



³⁴ See European Central Bank, ‘Euro Area Yield Curves’ (accessed 16 December 2019)

https://www.ecb.europa.eu/stats/financial_markets_and_interest_rates/euro_area_yield_curves/html/index.en.html.

Source: ESAs Consultation Paper, p. 22



Source: BETTER FINANCE [PRIIPs Position Paper](#), p. 4;

Reducing the chances that actual performance escapes the favourable and unfavourable scenarios' frame is important as it would not lead to overly optimistic or overly pessimistic forecasts. However, the new methodology **is applied not to the PRIIP**, but to the underlying portfolio. Therefore, the question is split:

- 1) will investors read and understand that those are **estimations** and are improbable?
- 2) will investors read and understand that those estimations are of an underlying benchmark, **and not of the PRIIP**, and returns may actually differ?

The disadvantage is that the proposed new formula changes the basis of the return estimation. Instead of using the historical prices or returns of the PRIIP itself, it is based on those of the asset classes the PRIIP invests in. As such, the new returns, if slightly less unrealistic, generalise across PRIIPs since two products investing in the CAC40 index will have almost the same expected return at RHP - what will differ is the net return, due to costs. As such, this new approach eliminates the element of **comparability**, which is central to the PRIIPs KID. This is because the risk-free rate (sovereign bond curve) and the dividend yield will be the same for both (asset class yield curve).

Return estimations are still inaccurate. If we cannot know now whether forecasts will prove correct or not (since they are in the future), academic literature, stakeholders' research and BETTER FINANCE's own computations have proved that returns cannot be accurately predicted.

In our opinion, **future performance accuracy is unreachable, irrespective of the method applied.** If on certain occasions the return estimation were "bullseye", we believe this is due to luck, not science.

MiFID II warns that past performance is not a reliable indicator of future results, yet future results are calculated precisely on the basis of past performance.

What is more, the more volatile a security is, the longer past performance is needed to reduce the standard error band in the return distribution. For instance, for some S&P Indices, in order to predict the returns within a +/- 0.5% interval of the sample mean, we calculated a

necessary 992 to 4800 years of historical returns of equities.³⁵ Nevertheless, securities generally have longer trading history than investment products. By generalising on asset classes, it may prove easier to obtain longer track records, which do make the return estimations narrower, but of the underlying portfolio, not of the PRIIP.

A potential amendment to the proposed methodology would be to use the product of the risk-free rate as a common denominator for all securities in the portfolio that have the same domicile and the yield curve (risk premia) for each individual security. However, this would raise the issue of data availability, as the PRIIP manufacturer would need to obtain the historical prices and calculate the yield curve for each individual holding in part (with some exceptions). This would have the advantage of individualising each PRIIP.

Therefore, BETTER FINANCE proposes an alternative methodology to present appropriate performance scenarios (see answer to Question 22 below).

Question 11. The ESAs are aware that historical dividend rates can be averaged over different time spans or that expected dividend rates can be read from market data providers or obtained from analyst reports. How should the expected dividend rates be determined?

The expected dividend rates must be estimated from the full price history available for each security class. As indicated above, in statistical probability the higher the number of observations (in this case, the historical returns – for Total Return PRIIPs – or prices – for Price Return PRIIPs) the lower the standard deviation (and, thus, the standard error band) in the estimated return distribution.

Therefore, the ESAs should require PRIIP manufacturers to obtain the full price or return history of the securities for which they are estimating returns. In the case of a more generalist model (as presented in the consultation paper), this could be read from published indices, provided that the ESAs lay down guidelines in order to not promote too divergent use of indices.

Question 12. How should share buyback rates be estimated?

N/A.

Question 13. Do you agree with the approach for money-market funds? Are there other assets which may require a similar, specific provisions?

N/A.

Question 14. The methodology proposes that the future variance be estimated from the 5-year history of daily returns. Should the volatility implied by option prices be used instead? If so, what estimate should be used if option prices are not available for a particular asset (equities namely)?

N/A.

Compensatory mechanisms

Question 15. Do you think compensatory mechanisms for unforeseen methodological faults are needed? If yes, please explain why.

³⁵ For n (the number of years) = $\left(\frac{\sigma_{\text{sample}} \times 1.96}{0.005}\right)^2$, where σ_{sample} is the standard deviation of the observed returns.

If the current approach (stochastic model for estimating results) would be kept, then a compensatory mechanism for correcting overly optimistic or pessimistic returns generated should be put in place.

As the ESAs have indicated, the mechanism is necessary to lower the maximum return to match the historic high and raise the minimum return to match the historic low of the product. However, considering that the new approach changed the growth estimator from the average lognormal return of the PRIIP (M1) to the expected rate of return of the underlying assets (g), the compensatory mechanism poses significant methodological challenges.

With the current methodology to estimate returns, the compensatory mechanism could have been used as the High- or Low-Watermark of the PRIIP's performance since inception. To give more accuracy, the maximum and minimum caps could have been averaged from all similar products in the same domicile, task which can be assigned to national competent authorities or the ESAs.

However, the new approach would mandate establishing compensatory mechanisms for each security class individually, taking into account their specificities and places of domicile. While it is still achievable, the ESAs must consider whether the approach (as presented on page 25 of the Consultation Paper) would not return conceptual inconsistencies in the return estimations.

Question 16. Do you favour any of the options above? If so, which ones? How would you ensure that the information in the KID remains comparable for all products?

N/A.

Question 17. Are there any other compensatory mechanisms that could address unforeseen methodological faults? If yes, please explain the mechanism; explain how it ensures that scenario information in the KID allows investors to compare PRIIPs, and explain how the information for similar products from different manufacturers remains sufficiently consistent.

N/A.

Maximum growth approach

Question 18. What are your views on the use of a simplified approach such as the one detailed above, instead of the use of probabilistic methodologies with more granular asset specific requirements?

This approach is similar with the maximum and minimum caps compensatory mechanism and presents the same methodological challenges. However, for mixed-assets products, we doubt whether it would actually help retail investors since they would need to calculate weighted returns in order to obtain a full picture of the PRIIP.

Question 19. Do you consider the use of a single table of growth rates appropriate? If no, how should the methodology be amended?

Yes, BETTER FINANCE believes this approach would be appropriate as a last measure – see answer for Question 18 above.

Question 20. More generally, do your views about the use of a probabilistic methodology vary depending on the type of product (e.g. structured products vs non-structured products, short-term vs long-term products)? For which type of products do you see more challenges to define a probabilistic methodology and to present the results to investors?

We believe that probabilistic methodologies are similar in terms of return accuracy, reason for which their use does not depend on the type of product. The presentation of outcomes for retail investors is similar for all types of products and formulae: it must be kept simple. Therefore, no further explanations should be given under the performance section other than the return estimations themselves.

Other alternative methodologies

Question 21. Do you think these alternative approaches should be further assessed? If yes, what evidence can you provide to support these approaches or aspects of them?

Estimating returns has proven so far – to our knowledge – inaccurate, and all the methodologies explored (the current one, the new one, others proposed by stakeholders) have inherent issues or limitations. The risk is that, while displaying certain advantages, other alternative methodologies (such as a maximum growth table etc.) create many more issues than those they solve. Evidently, if the ESAs would choose one of them, further prescription is necessary and, thus, further consultations would be necessary.

The purpose of the KID is to be simple, understandable, and concise. Therefore, the simplest methodology available should be explored – in this sense, our answer to Question 22 below provides our alternative proposal for performance scenarios.

Question 22. Are there any other approaches that should be considered? What evidence are you able to provide to support these other approaches?

BETTER FINANCE proposes to replace the probabilistic (stochastic) estimations of returns with illustrative scenarios since these would be less misleading, would not build on past returns and would be easier to couple with historical performance.

Disclosing estimated figures of profit at the recommended holding period (RHP) has a very high potential of giving rise to false expectations for retail investors. Moreover, it is difficult to mitigate the confusion created from publishing past performance and the warning attached to it and then disclose return estimations based on past performance.

On the other hand, illustrative scenarios would not attempt in predicting the future, but would give reasonable expectations to the retail investor on what can happen with a PRIIP during three or four scenarios: abnormal (positive or negative returns), significant losses or moderate performances.

We believe that meaningful information for retail savers is the one that prepares them for different, most likely, market evolutions – such as favourable, stress, moderate etc – without emphasising any particular level of return. Illustrative scenarios also have the advantage of providing some form of financial education and incentivising the retail saver to engage more often with its product and track its performance.

An explanation of what can be expected from the PRIIP during certain circumstances, however, must be kept simple, short and concise, avoiding jargon or technical language. Being aware of the pitfalls of providing too much narrative explanations, the illustrative scenarios must not appear as “chunks” of text, and should be accompanied by graphical illustrations (exemplificative only).

In our view, the simplest manner to achieve this illustrative scenario presentation is by not attaching figures to it – otherwise the door is opened to the same challenges as with probabilistic (stochastic) scenarios. The ESAs proposals consider describing an illustrative scenario as a drop or increase in the market (index) of the PRIIP and showing how the product would behave in such conditions.

We believe it to be a risky approach and to give rise to the same debate held so far on the method to achieve greater accuracy in return estimations; potentially, even worse, as correlating the decrease of the market with an accurate decrease of the product may prove more difficult than the current approach.

Therefore, BETTER FINANCE strongly advises the ESAs to replace probabilistic scenarios with illustrative ones (narrative only, maximum 2-3 lines), which would also be compatible with presentation of past performance (see answer to Question 26 below).

Illustrative scenarios for structured products

Question 23. Do you think illustrative scenarios should be included in the KID as well as probabilistic scenarios for structured products?

No, we believe that this double wrapping of information requires additional explanations on the relationship between them (illustrative and probabilistic scenarios) and does not help the investor better understand the product, nor the limitations of those scenarios. The KID for structured products, as for all other, should only present illustrative scenarios.

Question 24. If not, do you think illustrative scenarios should replace probabilistic scenarios for structured products?

Yes, illustrative scenarios should replace probabilistic scenarios – see answer to Question 23.

Question 25. Do you agree with this approach to define PRIIPs which would show illustrative performance scenarios using the existing definition of Category 3 PRIIPs? If not, why not? Where relevant, please explain why this approach would not be appropriate for certain types of Category 3 PRIIPs?

Yes, see answers for Questions 21 & 22 above.

5. Inclusion of past performance

Short summary: The ESAs are considering reintroducing past performance presentation for Category 2 PRIIPs (funds and IBIPs) in the PRIIPs KID in view of the transition of UCITS from the KIID to the KID. **Questions analysed:** 26 – 32.

Question 26. Would you be in favour of including information on past performance in the KID?

Yes, BETTER FINANCE has always advocated in favour of past performance only for one clear reason: while past performance is not a reliable indicator of future results, it has the characteristic of showing the investor whether the product manager has reached its stated investment objectives in the past.

Accompanied by the short, concise and prominent warning that historical returns should not be used in any way to estimate future outcomes – as is currently the case for the UCITS KIID – it constitutes a clear and accurate measure for the retail saver to evaluate the past performance of the product manufacturer and provides a comparison basis for other products. Moreover, past performance must be accompanied by that of the market index benchmark (see answer to Question 32 below).

If **past performance** is not the silver bullet in making an informed investment decision – the KID is a holistic reporting document and all of its parts must be considered – **it is pivotal**. However, the function of regulatory reporting documents, such as the KID, is to ensure that the information and data comprised therein are accurate (reflect either the reality or known facts, just like a

certification process) and it is the duty of law and regulatory authorities to achieve this function. It is for this reason that by including future performance, and not past performance, law eliminates the accurate reporting nature of the KID and reduces it to “reasonable assumptions”, which would not be the case with past performance.

Therefore, in order to build to the accurate nature of the KID, past performance information in comparison with a relevant benchmark must be included.

If a product does not have past performance (because it is new or has been launched too recently), it should not be presented. However, if the product has past performance, the only exception to this rule could be admitted for those structured products that are made *intuitu personae* and do not allow the investor or the product manufacturer to sell or buy it until maturity.

Question 27. Would your answer to the previous question be different if it were possible to amend Article 6(4) of the PRIIPs Regulation?

No, the provisions of Article 6(4) PRIIPs Regulation do not affect inclusion of past performance from the point of view of the length, conciseness or accessibility of the PRIIPs KID.

Question 28. Do you think that it can be more appropriate to show past performance in the form of an average (as shown in the ESA proposal for consumer testing) for certain types of PRIIPs? If so, for exactly which types of PRIIPs?

No, we do not – past performance disclosure must be harmonised for all types of PRIIPs. For most used PRIIPs, as done for UCITS funds (including money market funds with very short RHPs and including target retirement funds with very long RHPs), the longer the disclosed track record is the better. This is because it is then more likely to track different cycles (like bull and bear for stocks for example), and also shows the persistence (or not) of the manager’s ability to perform and to meet his own investment objective.

The other crucial disclosure is to have the past performance of the benchmark chosen by the PRIIP manager alongside that of the product itself, like for UCITS funds. Indeed, the absolute past performance of a given PRIIP has little meaning if not compared of its benchmark (investment objective).

Question 29. Do you have any comments on the statement that would supplement the display of past performance (e.g. with regard to the presentation of costs which are not included in the net asset value (NAV))?

BETTER FINANCE agrees with the text as used in the KIID Regulation, except the two additions on the market conditions and use of past performance. While, in principle, we believe that warning against hyperbolising historical returns would prove advantageous for the retail investor, the third sentence does not particularly do that. In the current conditions it would cause even more confusion.

Therefore, the prominent warning should be displayed in bigger font and different colour (preferably red) and read:

“Past performance is not a reliable indicator of future results”.

However, we take this opportunity to comment on the narrative descriptions and warning in reference to future performance, since there is no corresponding question.

The general comment (pages 4-10) and the answer to Question 26 lay the foundation for this comment. Studies have revealed that investors do not respond correctly or positively to large amounts of information, including text descriptions. Considering that the function of the KID is to

provide reliable and accurate information for the retail saver, further descriptions (as suggested by other stakeholders or policy makers) or warnings in the performance scenarios' section will lead to information overload and confusion.

The KID must be provided by product manufacturers by virtue of the law, and it is currently completely prescribed and standardised (as opposed to commercial communications, which comprise limitations only). Moreover, it is not the task of non-professional savers to research, verify and validate the information presented in the KID, nor to know and evaluate the methodology to produce such estimations.

Therefore, the only prominent warning that should accompany the performance scenarios' section is the following:

"The above returns are what we reasonably assume will happen in [x] years"

Question 30. Are you of the opinion that an additional narrative is required to explain the relationship between past performance and future performance scenarios?

Considering the current amount of information and narrative explanations comprised in the PRIIPs KID, it would not have added value for retail savers to include another warning on the relationship between past and future performance – nor can such a relationship be concisely enough explained (one or two sentences).

Therefore, BETTER FINANCE opposes such an addition. Moreover, as stated in the answer to question 1, we deem it also important for the ESAs to use the already available behavioural insights and behavioural experiments undertaken by some of the competent authorities as to the effectiveness of too long disclosures.

Question 31. Do you see merit in further specifying the cases where the UCITS/AIF should be considered as being managed in reference to a benchmark, taking into account the provisions of the ESMA Questions and Answers on the application of the UCITS Directive?

We believe that the recent (April 2019) ESMA Q&As on UCITS (in relation to the past performance presented in the KIID) addressing the issues raised by Article 7(1)(d) of the KIID Regulation of when a UCITS/AIF is managed in reference to a benchmark are sufficiently clear, prescriptive and identify precisely the practical issues arising from the obligation to disclose the benchmark and publish its past performance along that of the UCITS/AIF.

However, as we indicated in the ESMA Public Consultation on Performance Fees, divergent practices at national level require directly enforceable provisions from the ESAs, not merely soft law. Therefore, while there is no need to expand the guidelines identified by ESMA, it would be beneficial to award those with a stronger legal force and include them in the Level 2 legislation on PRIIPs.

Question 32. Do you see the need to add additional provisions for linear unit-linked insurance-based investment products or linear internal funds?

N/A.

6. Methodology for calculation and presentation of cost information

Short summary: The ESAs consider that the current summary cost indicator, based on the Reduction-in-Yield, is the most meaningful way to convey the total costs incurred by the retail investor. However, the ESAs are proposing 4 options to address

the presentation of costs methodology, a play between showing the RiY and monetary terms; the ESAs prefer Option 3 and, secondly, Option 4. **Questions analysed:** 33 – 43.

Question 33. *Do you agree that a fixed intermediate time period / exit point should be used instead of the current half the recommended holding period to better facilitate comparability?*

Yes, see answer to Question 7 above.

Question 34. *In this case (of a fixed intermediate time period), do you agree to show costs if the investor would exit after 5 years for all PRIIPs with a recommended holding period of at least 8 years? Or do you prefer a different approach such as:*

- *Applying this approach (i.e. showing also the costs of exit at 5 years) only for PRIIPs with a longer recommended holding period, for example at least 10 years*
- *For longer term products (e.g. above 15 years) showing exit costs at a different fixed time period (e.g. 10 years instead of 5 years)?*

The answers to Question 7 above particularly address this question as well.

Question 35. *Do you think it would be relevant to either (i) use an annual average cost figure at the recommended holding period, or (ii) to present both an annual average cost figure and a total (accumulated) costs figure?*

BETTER FINANCE strongly advises the ESAs to consider either standardising the recommended holding periods or harmonising an intermediary point which would be common to all products. Presenting an average cost figure, as proposed in the Consultation Paper, would not improve the aspect of comparability at all, but would have the adverse effect of diluting costs over time and misleading investors to more long-term products without taking into account suitability.

The ESAs have correctly identified that presenting too many cost figures may lead to information overload, reason for which we **suggest to** keep the summary cost indicator simple and understandable. Therefore, the ESAs should prescribe only the second option.

36. *Do you think that it would be helpful, in particular for MiFID products, to also include the total costs as a percentage of the investment amount?*

Yes, costs must be presented both in percentage (%) and monetary terms for the retail investor. Concerning the correlation with the MiFID II disclosure, which is actual costs charged by the product manufacturer, the misalignment is not addressed by merely including costs in percentage terms. Moreover, this is not merely a policy preference of BETTER FINANCE, but the actual requirement in the PRIIPs Regulation, Article 8(3)(f).

This constitutes a serious issue since many product manufacturers will (and are) disclosing “two sides of the same face” but in different figures. The ESAs should have analysed the disclosure requirements under MiFID II and align the PRIIPs provisions with the former, so as the information – whatever the source – about a financial product is the same.

In particular, MiFID II does not require product manufacturers to generate performance estimations to calculate costs, which gives completely different temporal dimensions to the presentation of fees and charges, albeit the fixed or pro-rata costs are the same. What is more, whereas MiFID II requires disclosure of the costs taken from the investment, PRIIPs discloses not the costs, but the **impact on return**, illustrated by a Reduction-in-Yield, due to costs.

Therefore, this distinction is a conceptual difference imposed by EU law. We are happy, however, that the ESAs have informally manifested intent to solve the disclosure discrepancies between

PRIIPs and MiFID II, but much more work – actually, a distinct review – would have been needed in order to address these abovementioned issues.

Lastly, we also believe that the RiY is not calculated accordingly for the purposes of communicating information to retail savers. Individual, non-professional and small investors do not have extended knowledge or experience with financial products and, as such – on most occasions – lack a scale of size to determine whether the RiY, calculated as the difference in the gross and net internal rate of return, is large or not (in other words, whether the PRIIP is expensive or cheap). However, what is important is to show the cumulative effect or impact of costs on the gross return for the saver (see answer to Question 41 below).

37. In this context, are there PRIIPs for which both performance fees and carried interests are applied?

N/A.

38. Do you agree with this analysis from the ESAs? If yes, what are your views on the extent to which fees related to the management of the underlying real estate assets, i.e. the properties themselves, should be taken into account in the calculation of the cost indicators?

N/A.

Question 39. Do you agree with the ESAs' preferred option 3 to revise the cost tables?

We do not agree with Option 3 – instead, BETTER FINANCE advises the ESAs to choose Option 4. First, removing the cost figures in monetary terms from any cost disclosure – at the moment – is undesirable especially taking into account the general low level of understanding or knowledge of individual, non-professional savers of percentages and compounding terms in financial services. As such, monetary terms must be kept in all PRIIPs costs disclosures.

Second, Option 3 extends the amount of information presented in the breakdown of costs and runs counter the stated risk of information overload – recognised even by the ESAs on page 36 concerning the summary cost indicator. We do not believe that in a short and concise document as the KID additional explanations or details on the costs breakdown or categories is needed for the moment.

Last, the proposal for Option 3 adds four more figures per cost categories (assumedly, after 1 year and at an intermediary point in time) which will purely replicate the misleading, confusing and otherwise detrimental effects generated by the summary cost indicator (RiY) of Table 1.

Question 40. If not, which option do you prefer, and why?

The purpose of the KID is to be simple and concise, reason for which we prefer (out of the four presented) Option 4, with the amendment that costs in percentage terms should also be presented.

The additional explanations should be removed, and product manufacturers can make a cross reference underneath the table to the Prospectus or the source where the retail saver can obtain more information about the description and structure of each category of cost.

Question 41. In particular, do you think that the proposed changes to the presentation of the impact of costs on the return in percentage terms (i.e. including reduction in return before and after costs) is an improvement on the current presentation?

A more meaningful manner to present the impact of costs would have been to display the cumulative reduction of the gross return due to costs, such as: gross performance (before costs): 175%; net performance (after costs): 125% => cumulative reduction due to costs of 50 percentage points out of the total profit, which represents 66%, or 6€ out of 10€.

This would give a better understanding of the scale size of costs for retail investors, rather than a difference between the annualized gross and net returns at different periods.

Question 42. Do you have other comments on the proposed changes to the cost tables?

Yes: we reiterate our call to remove this incomprehensible and confusing Reduction-in-Yield measurement at different holding periods, based on an undisclosed performance scenario, and replace it with actual costs, as is currently the case with UCITS KIID, or with the contractual costs. For those products to which costs are an unknown aspect before conclusion of the contract, the KID should clearly mention “**unknown**” instead of producing estimates.

The introduction of the RiY does not necessitate a review of Level 1 as it is a pure discretionary choice of the EC and of the ESAs. According to the relevant provision in the PRIIPs Regulation, the KID must only disclose costs “by means of summary indicators and [...] total aggregated costs”. As such, modifying the manner to calculate and present costs may prove the simplest task of the ESAs in this Level 2 review process.

Transaction costs

Question 43. What are your views on the appropriate levels of these thresholds? Please provide a justification for your response.

BETTER FINANCE believes that transaction costs should be eliminated since they represent an implicit (theoretical) market impact on the trade and for the return of the retail investor. BETTER FINANCE proposes to replace this cost indication (which is not actually a cost) by the portfolio turnover rate (where available) as a proxy for the product manager’s activity.

7. UCITS exemption under PRIIPs

Short summary: The ESAs raise the issue that, as of 1 January 2022, the UCITS KIID will no longer be offered to retail investors (being replaced by the PRIIPs KID), but only to professional investors – as the law stands today. In view of regulatory proposals the ESAs are envisaging to put forward to the co-legislators, this section seeks to answer whether such a duality should be avoided or not. **Questions analysed:** 44 – 49.

Question 44. If UCITS would fall in the scope of the PRIIPs Regulation, do you agree that the coexistence of the UCITS KII (provided to professional investors under the UCITS Directive) and the PRIIPs KID (provided to retail investors under the PRIIPs Regulation) would be a negative outcome

in terms of overall clarity and understandability of the EU disclosure requirements? Are you of the view that the co-legislators should therefore reconsider the need for professional investors to receive a UCITS KII, as the coexistence of a PRIIPs KID together with a UCITS KII (even if not targeted to the same types of investors) would indeed be confusing, given the differences in the way information on costs, risks and performance are presented in the documents? Alternatively, are you of the view that professional investors under the UCITS Directive should receive a PRIIPs KID (if UCITS would fall in the scope of the PRIIPs Regulation)?

BETTER FINANCE reiterates its position that the UCITS KIID is an example of proper pre-contractual disclosure for investment products and advises the ESAs to take the opportunity to keep in place this document since it will be the last source (for a part of the market only – UCITS and some AIFs) of actual performance and costs data.

Therefore, professional investors should receive only the UCITS KIID, and retail investors should have the possibility to opt-out from the UCITS PRIIPs KID.

In absence of this standardised document, the ESAs will no longer be able to use documents prescribed by EU law to report on the cost and past performance of the retail investment products in their scope, nor to fulfil the objective of creating a public database and promote transparency.

In absence of legislative changes in this regard, BETTER FINANCE proposes to the ESAs to introduce a specific provision in the PRIIPs Level 2 regulation by which retail investors can opt-out from the PRIIPs KID and be provided, instead, the UCITS KIID, which will be mandatorily disclosed only to professional investors.

To circumstantiate, the right to opt-out should be in force for UCITS and AIFs either until the Level I PRIIPs review would be completed, or it should have a permanent nature (regardless of the result of the PRIIPs Level I review).

Question 45. What are your views on the issue mentioned above for regular savings plans and the potential ways to address this issue?

The difference in wording between the Guidelines for UCITS and Article 13(4) PRIIPs Regulation is justified from the point of view of retail savers: whereas the UCITS KIID focuses on past data – which the investor already received before entering the contract – the PRIIPs KID shows future costs and returns, reason for which it is necessary to re-communicate them.

However, if substantial changes are made to either the KIID or KID, the retail client should be informed of them and receive again a KIID or KID. Delivery of the PRIIPs KID should also consider whether the additional investments form a new contract, subscribe a new PRIIP or change the already existing choices made with the current (past) PRIIP.

BETTER FINANCE is of the opinion that, considering the nature of the information disclosed in the PRIIPs KID (based on assumptions), changes to the initial subscription plan that do not affect the investment choice/ the composition of the product or its costs/ the risk profile/ the sector or focus of assets, but only non-essential elements (such as purely the investment amount) which do not give rise to a change in the treatment or contractual terms for the retail investor should not oblige the product manufacturer or person responsible *ex officio* to send the new PRIIP KID.

Based on the wording of Article 13(4) PRIIPs Regulation, we do not believe that it would be inconsistent with the current guidelines (Q2c & A2c) for the UCITS Directive. Nevertheless, for reasons of legal certainty, the PRIIPs Level 2 implementing provisions should make these specifications.

Question 46. Do you agree that these requirements from Article 4 should be extended to all types of PRIIPs, or would you consider that it should be restricted to Management Company of UCITS or AIFs?

Yes, all PRIIPs should provide information (if available) concerning the share class, group of the management company, or identification codes, etc., in the KID.

Question 47. Do you agree that this requirement should be extended to all types of PRIIPs, or would you consider that it should be restricted to Management Company of UCITS or AIF?

Yes, the purpose of the KID is to be comprehensible and easy to read for the average saver, and signposting to a Glossary of Terms may enhance it, especially concerning complex products. Concerning the other requirements clarified by Questions 5 & 7 of Section II of the UCITS Q&A, BETTER FINANCE believes it would be beneficial to be also included for all PRIIPs.

Question 48. Do you agree that these requirements should be extended to all types of PRIIPs, or would you consider that they should be restricted to the Management Company of the UCITS or AIF?

In light of the ongoing efforts of the ESAs and National Competent Authorities (NCAs) to combat closet indexing, we firmly support the proposal to include the provisions of Article 7 KIID Regulation (583/2010) in the KID, in particular in the past performance section (which should be included).

Comparisons with the benchmark fulfil the purpose of past performance, i.e. to show whether the product manufacturer has reached its stated investment objectives. In addition, when it is not related directly to a market index benchmark, provide the retail saver with meaningful comparison on the performance of the product manager. BETTER FINANCE has justified at-length this necessity on several occasions.³⁶

The work of ESMA³⁷ in clarifying the obligations for identifying products managed in reference to a benchmark will be key for this process and should be extended to all types of PRIIPs where such comparison is relevant for the retail saver.

Therefore, BETTER FINANCE supports including Articles 7, 9, 15-21 of the KIID Regulation in the PRIIPs implementing measures and extending their application to all PRIIPs (where relevant) – we are aware of the fact that some PRIIPs may have characteristics that do not mandate relevant publication of such information, but this must be decided on a case-by-case basis.

Question 49. Do you have any comments on the proposed approaches in relation to the analysis and proposals in this Section, and in particular on the extent to which some of the abovementioned requirements should be extended to other types of PRIIPs?

N/A.

8. Provisions for Multi-Option Products (MOPs)

Short summary: The ESAs are considering how to better communicate the costs for Multi-Option Products (MOPs) in the generic PRIIPs KID. One proposal is, instead of presenting a range of costs (current approach, minimum-maximum), of calculating the

³⁶ See first the BETTER FINANCE, 'Benchmark Disclosure Compliance Report' (2018, <https://betterfinance.eu/wp-content/uploads/PR-Benchmark-Disclosure-Compliance-Research-040618.pdf>) pages 12-17; see BETTER FINANCE, 'ESMA reinforces Benchmark Disclosure Requirements for UCITS' (2019, https://betterfinance.eu/article/esma-reinforces-benchmark-disclosure-requirements-for-ucits/#_ftn3);

³⁷ ESMA Q&A on the Application of the UCITS Directive, 29 March 2019, ESMA34-43-392, Section II, Questions 4 (b and cbis) and Questions 8 (a, b, and c).

total cost of the most selected combination of investment options, while keeping the ranges for the breakdown table. **Questions analysed:** 50 – 54.

Question 50. Do you think this proposal would be an improvement on the current approach?

The ESAs rightfully noted that a generic KID, offering ranges of costs for MOPs, make it “difficult for the investor to identify the total costs related to a particular investment option”.³⁸ The purpose of the KID is to show the total aggregated cost of the investment product, i.e. the wrapper and the underlying supports, which is currently not the case for most MOPs. However, the ESAs have not mentioned other significant issues generated for retail savers using MOPs, described below.

Requiring the saver to use the different documents (generic KID and KIIs or PIS of the supports) to compute costs is on many instances impossible. First, the KID produces cost estimations and some PIS (product information sheets) for the underlying options use past costs, thus impossible to compute.

Second, it is very difficult to understand what is the cost of the wrapper (contract) and what are the costs of the underlying options due to the different disclosure (and aggregation) requirements between documents.

Third, and **most importantly**, if the wrapper PRIIP would have a RHP of 5 years and the support would have a RHP of 6 years, it will be mathematically impossible to deduce the total costs or the cost split (wrapper / support) for MOPs.

For BETTER FINANCE, the desired approach is to produce a separate KID for each investment option from the MOP as those generate a new, different, PRIIP. The separate KID, instead of the generic one, would fulfil the requirements of Article 8 and disclose the **full total cost** for the saver.

If this alternative is not chosen by the ESAs, then a breakeven solution could be to use the generic KID where the costs are differentiated in the generic KID between the wrapper and the underlying supports. The first table (SCI) would calculate the RiY as it is currently the case, but the cost breakdown table would add another line indicating the cost of the wrapper product:

This table shows the impact on return per year			
Contract cost	Wrapper cost	1%	The impact of the cost for entering this contract
	Entry costs	0.1% + [0.2% - 1%]	The impact of the cost for entering this contract and/or the supports
One-off costs	Exit costs	2% + [0.2% - 1%]	The impact of the cost for exiting this contract and/or any of the supports
	Ongoing costs

Source: BETTER FINANCE own composition

In order to enable savers to understand what the costs of the MOP are and how should he use the supporting PISs to calculate the total costs, the distinction between the costs of the wrapper and the costs of the supports must be made. Moreover, this would give clarity for the Table 1 (RiY) and would improve understanding of the cost structure for MOPs. BETTER FINANCE’s subsidiary proposal is a draft and can be further discussed and improved, but should not prejudice assessment of our clear indication, i.e. that a separate KID per option should be produced.

Question 51. Do you envisage significant practical challenges to apply this approach, for example for products which allow the investor to choose between a wide range or large number of options?

N/A.

³⁸ Page 51 of the Consultation Paper.

Question 52. Do you see any risks or issues arising from this approach in relation to consumer understanding, for instance whether the consumer will understand that other combinations of investment options are also possible?

This approach carries two risks in terms of consumer understanding. First, the requirement of Article 8 PRIIPs Regulation is not fulfilled as the retail saver will not get the full cost of the PRIIPs offered, but for four investment options which may prove in many circumstances not to be the most suitable or the recommended investment option for the saver.

Second, the client may be biased towards the four presented options due to the narrative and presentation of costs, and may be prone to consider that those four are the “best” products to invest in.

Should the ESAs choose this approach, a clear warning must be put in place to inform the saver that those are exemplificative illustrations, and the actual cost of the saver’s choice of investment option may or will differ.

Question 53. Do you think this proposal would be an improvement on the current approach?

It would bring a slight improvement, but it falls short of the legal requirements for the KID – see answer for Question 50 above.

Question 54. Are there other approaches or revisions to the requirements for MOPs that should be considered?

Yes, our alternative proposals are highlighted in the answer for Question 50 above.

9. Cost-benefit analysis

This section is not applicable for BETTER FINANCE.

Question 55. Do you have any comments on the preliminary assessment of costs and benefits?

N/A.

Question 56. Are you able to provide information on the implementation costs of the proposed changes, in particular regarding, (1) the proposed revised methodology for performance scenarios (using a reference rate and asset specific risk premia), and (2) the overall changes to the KID template?

N/A.

Question 57. Are there significant benefits or costs you are aware of that have not been addressed?

N/A.