**Reply form for the
Technical Discussion Paper on PRIIPs**

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'.

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[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	European Structured Investment Products Association
Activity	Banking sector
Are you representing an association?	☒
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:
< ESMA_COMMENT_PRIIPs_1>
TYPE YOUR TEXT HERE
< 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>
Regarding the risk indicator:
EUSIPA clearly rejects approaches a) and b). EUSIPA also has doubts about approach d).

Approach a) is already too biased as past performance does not necessarily reflect the future.
EUSIPA rejects approach b) as well. Though option b) is more observable (manufacturers all use the same historical data), it is less accurate as the models used for product pricing and risk are using historical data. Using such it is not representative of future performance and will not show the actual risks. It also creates a mismatch between product risk indicator computation and product valuation which is done with forward looking parameters available in the market. Finally it is difficult to implement as each PRIIP would have to be "valued twice", with historical parameters for risk indicator, and with actual market parameters for the actual pricing/trading of the product.

Approach d) may introduce serious issues for regulators to ensure that the right parameters are always used consistently throughout the EU markets in the right context (in particular considering the wide range of PRIIPs). Independent of this view, EUSIPA could support ESA guidelines on selected parameters (e.g. for the computation of risk premiums) if market evidence shows that there an inconsistency between issuers on the use of such.

Generally we wish to underline that prescribing a too sophisticated approach (e.g. approach b) or d)) will result in increased costs which are not out-weighted by the benefits for investors of a risk indicator with higher comparability.

Regarding performances scenarios:

EUSIPA clearly rejects a probabilistic approach.
Our view is that the most relevant criterion for a performance scenario is the illustrative approach as it is aimed at the final investor. The "what if"-prescribed approach seems therefore the most suitable (see our answer to question 15). Its presentation would enable the investor to easily see how the product would perform under a selection of key hypothetical market situations that directly impact the various product features (e.g. triggering of a barrier). <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>
We believe that the choice of the model used to generate a distribution of return should be left to the discretion of the manufacturers considering that internal pricing models are already used for accounting purposes and, as such, are audited and validated by prudential regulators.
The manufacturer could nevertheless be required to disclose the model name and the assumptions upon request of the ESAs. Parameters should be based on current observable market prices of derivatives.
<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>
EUSIPA takes the view that manufacturers should not be required to display a benchmark in performance scenarios, for the following reasons:

1) Risk-free rates in the Eurozone highly vary between countries (e.g. deposit rates in Spain between 2010 to 2013 were much higher than in Germany) which means that investors in each country instinctively decide based on different government/risk-free rate benchmarks.
2) The choice of the appropriate benchmark depends on each investor's risk appetite and risk premium. <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>
Under the assumption that performance scenarios are not prescribed as probabilistic, EUSIPA has no clear preference for any of the options.
However, despite this not being the EUSIPA position, in case probabilistic performance scenarios are being prescribed, EUSIPA would strongly be in favour of including risk premiums. In such case (of probabilistic scenarios), a growth rate set to the risk free rate (option a)) would not be satisfactory for equities and commodities. Condition c) could in this case be problematic if the risk premium is reviewed too frequently. EUSIPA would in such case prefer condition b) with the asset growing at risk free rate adjusted by an asset specific risk premium, set by the regulators with prescriptive conditions if market evidence confirms that such risk premium is not applied consistently across issuers. <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>
As for performance scenarios, EUSIPA supports the approach set out under scenario C.
For products with a fixed maturity, the entire term until maturity should be used. For open-end products a standardised holding period could be used, As for the risk indicator, EUSIPA agrees that a timeframe in line with to option c should at least be used for products which are illiquid and cannot be exited prior to maturity.
EUSIPA would also support the additional inclusion of a narrative text that explains the possible variation in risk over time. <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>
EUSIPA wishes to underline that the credit risk of the PRIIP hinges on the risk for the investor of a failure of the issuer or the guarantor, if any. It is not dependent on the default risk of the underlying assets, which is accounted for in the market risk.
EUSIPA supports credit risk to be included in the summary risk indicator. <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>
EUSIPA agrees that liquidity risk should be reflected in the risk indicator. It should be fully integrated in a risk indicator as a risk along credit and market risks.
In the way to apprehend liquidity risk, EUSIPA is convinced that narratives are much more accurate than the use of a quantitative liquidity indicator. (See also our answer to question 8 below.) <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>
As stated in our answer to the previous question, EUSIPA does not consider quantitative measures to be appropriate for apprehending liquidity risk as the envisaged tools refer only imprecisely to liquidity risk. For example, bid-offer spreads integrate global hedging costs and not only liquidity costs. A precise narrative of liquidity risks borne by the investor seems therefore more accurate.
EUSIPA agrees that the narrative should refer to the 4 criteria mentioned in the TDP in the section "qualitative liquidity measures". For reference, these criteria are:
 (i) a product is traded or will be traded on a regulated market or MTF
(ii) a liquidity provider exists (either manufacturer or other parties)
(iii) market rules ensure liquidity under normal conditions and/or,
(iv) when regular redemption dates are offered throughout the life of the product under normal market conditions.

Should cost and exit penalties for early redemptions be considered a component of the liquidity risk and hence, be used to define a product as liquid or not for the KID purpose?

EUSIPA does not support this view. Liquidity is in our view a different topic than exit penalties. Exit penalties should be dealt with in the cost section of the KID. <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>
EUSIPA clearly rejects option 1 as it has several material drawbacks:
1. There is no quantitative rationale in the scale. It is less a risk measure than a product classification, which does not bring clarity to the investor.
The major flaw of option 1 is the general absence of quantitative information on market risk. In our eyes this would be an important hindrance especially (though not only) on the secondary market where quantitative changes in the risk profile are important investor information.
As a consequence, EUSIPA believes the main difficulty with the model set out under option 1 to be a risk for an arbitrary classification and the lack of visibility and differentiation between crucial variables that influences the potential yield for investors (for example payoff mechanism, underlying, worst off-features and others).
The model could even lead to a significant part of the packaged investment products landscape ending up regularly in a medium risk class (such as class 3) with no further differentiation, which, coupled with a lack of descriptive detail, adds hardly any value to final investors and financial advisers.
2. More specifically, option 1 runs the danger to create even an un-level playing field between different sorts of PRIIPs, for example between funds and structured products linked to funds: a bond fund has a risk class 2 as a non-structured PRIIP, while a 50% capital protected Note on the same bond fund (i.e. providing capital protection on the downside and a limited gearing on the upside) would fall into a higher risk class of 4.
Another example is that of a "delta1"-note collateralized by the bond/fund/shares (so free of issuer/credit risk) which according to the set out methodology would receive a risk rating of 5, which seems highly inadequate. The same goes for the given situation of an 80% capital protected product that would automatically be assigned to risk class 3 in the proposed classification.
3. As is evidently already from the outset, option 1 would also create further mismatches in the classification of products. Below are set out two examples:
- Example 1: Suppose there are two capital guaranteed products: one with a very high but very unlikely coupon, the other one with guaranteed coupon. Under the methodology promoted under option 1, these two products may have the same rating of 1, while their income profile is fundamentally different for an investor.
- Example 2: A 70% capital guaranteed with a call strike of 70% should not have same risk class of 5 as a product with the same 70% capital guarantee but with a call strike 100%. Indeed the first product gives the investor a much higher chance of receiving more than 70% capital back (it could even be a 100% capital back). To the contrary, the second product, the underlying needs to perform (call pay-out of at least 30%) for the investor to get his capital back.
4. Furthermore, for structured products the consideration of the strike level versus the capital guarantee is not sufficiently addressed under this approach. As for the assessment of "average loss" option 1 adds a quantitative measure but its limitation stems from the fact that it is based on historical period. As for volati-

lity, option 1 adds an appropriate quantitative measure but it requires setting up a new classification grid.
<ESMA_QUESTION_PRIIPs_9>

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

<ESMA_QUESTION_PRIIPs_10>
EUSIPA supports a quantitative approach to market risk measurement. EUSIPA also supports the inclusion of credit risk into a summary risk indicator, which could also have a multi-dimensional layout.
EUSIPA suggests that the risk indicator finally recommended by the ESAs to the European Commission takes into account, to the extent adequate and technically possible, the current risk measurement practices of financial product distributors in the EU with the aim to ensure coherence between future regulatory requirements and existing market standards.

EUSIPA would like to stress the following regarding option 2:
While for analytical reasons, market risk and credit risk are assessed separately, as calculation methodologies differ, the two components are nevertheless part of the same risk assessment. Merging the two risk measures in a single risk seems to us a mere question of presentation. This merging can be based on a maximum or on an average between the 2 indicators (market and risk measures). <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>
As mentioned in the reply to question 10, EUSIPA supports a quantitative approach to market risk measurement. EUSIPA also supports the inclusion of credit risk into a summary risk indicator which could also have a multi-dimensional layout.
<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>
EUSIPA would like to stress that with regard to the implementation of a quantitative risk measurement model, the manufacturer should have discretion as to the choice of the parameters to the widest extent possible, provided they are adequate to reflect the risks of the specific product and the specific market conditions. The final RTS should not require "full valuation". <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>
EUSIPA clearly rejects option 4.
A two-level risk indicator contradicts the idea behind a summary risk indicator as is requested under the PRIIPs regulation. It also runs a high danger of creating a judgmental bias at the investor level as retail customers might put an overly strong emphasis on the first risk level which will per definitionem not correspond with the final product risk. <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>

EUSIPA believes it of high importance that the risk scale provides for sufficient granularity to differentiate properly between different PRIIPs.
Both a scale ranging from 1 to 5 or from 1 to 7 would thus seem appropriate. <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>
EUSIPA is of the opinion that the most relevant criterion for a performance scenario is their illustrative purpose. For structured products, scenarios should help the client understand how the product works and how movements in the price of the underlying will affect returns. The "What-if" prescribed approach seems the most suitable. Level 3 guidelines could be published for each type of PRIIP (structured products, funds, insurance products) similar to the guidelines already in place for UCITS funds (CESR 10-1318). <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>
EUSIPA believes that it would be helpful if ESMA is to publish guidelines on performance scenarios should market evidence support the view that there is no coherence among issuers. <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>
EUSIPA is convinced that guidelines would be helpful but does not fully agree with the options presented in the TDP. We would like to make the following comments with regard to
- Option A: Past performances are not representative of future performance.
- Option B: Setting a fix growth rate of the underlying (for example 10%) does not seem appropriate as the level of the rate needs to be adapted according to the pay-off.

Generally, EUSIPA considers it useful if guidelines could be established for each type of PRIIPs in the light of CESR-1-1318 guidelines already in place for structured UCITS funds. Such guidelines should be adapted to pay-offs.

EUSIPA is of the opinion that in a what-if prescribed framework manufacturers should be allowed to manually draw performance scenarios respecting prescriptive guidelines, while having the option but not the obligation to automatise the display of performance scenarios by relying on some quantiles of the payoff distribution. Manufacturers wishing to automatise the display of performance scenarios by relying of some quantiles of the payoff distribution should be using an equity risk premium set by the ESA in a prescriptive manner if market evidence shows that there is no coherent application/use of risk premiums between issuers. (To illustrate: Usually an equity risk premium of 4% to 7% is appropriate for most shares.) <ESMA_QUESTION_PRIIPs_17>

18. Which percentiles do you think should be set?

<ESMA_QUESTION_PRIIPs_18>
EUSIPA would like to underline that percentiles are only relevant for manufacturer wishing to automatise the what-if prescribed scenarios – this should be an option, but not be mandatory. <ESMA_QUESTION_PRIIPs_18>

19. Do you have any views on possible combinations?

<ESMA_QUESTION_PRIIPs_19>
EUSIPA does not support combinations in above sense.
EUSIPA likes to stress that combinations of historical, hypothetical, and probabilistic scenarios could be difficult to understand for retail investors. They will also be heavier to implement as they involve a mix of automated computing and manual intervention on the KID. <ESMA_QUESTION_PRIIPs_19>

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

<ESMA_QUESTION_PRIIPs_20>
EUSIPA does not support this view.
Performance scenarios are exclusively focused on market risk. Moreover, the case of a default of the issuer is already handled in another section of the KID. EUSIPA draws attention to the fact that under current directives UCITS funds are not required to display default risks of the custodian in their performance scenarios. For comparability reasons this should consequently neither be considered for structured products or other non-fund products falling into the scope of the PRIIPs regulation. <ESMA_QUESTION_PRIIPs_20>

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

<ESMA_QUESTION_PRIIPs_21>
EUSIPA is of the opinion that redemption events should be considered in performance scenarios, but only insofar as they relate to automatic early redemption or a "holder put-ability" for a given value on fixed dates. Both these cases should also be verbally explained. Voluntary redemption understood as selling the product on the secondary market should not be considered in the scenarios. Such case should rather be dealt with in the KID section entitled "How long should I hold it and can I take my money out early?". <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>
EUSIPA does not support to show performance in the case of exit before the recommended holding period. The possibility and implications of an exit are already dealt with in other sections of the KID, namely those describing the product structure, its disadvantages (option to exit for the issuer) and liquidity aspects (exit cost) of the product.

Do you think that fair value should be the figure shown in the case of structured products, other bonds or AIFs?

EUSIPA does not believe that the fair value is an adequate measure relative to future performances. For a given scenario the fair value is difficult to compute (because of the conditional expectation) and should not be used for scenarios. For future periods, the very starting point of the scenario is uncertain and the retail client is likely to misinterpret the conditional expectation of the shown intermediate performance.

Do you see any other methodological issues in computing performance in several holding periods?

We believe it will be misinterpreted, and we do not see the benefit for retail investors. <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>
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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>
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<ESMA_QUESTION_PRIIPs_24>

25. Should these fees be further specified?

<ESMA_QUESTION_PRIIPs_25>
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<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>
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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>
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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>
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<ESMA_QUESTION_PRIIPs_28>

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

<ESMA_QUESTION_PRIIPs_29>
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<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>
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<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>
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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>
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<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>
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34. Is this description comprehensive?

<ESMA_QUESTION_PRIIPs_34>
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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>
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<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 (book-

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

<ESMA_QUESTION_PRIIPs_37>
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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>
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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>
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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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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>
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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?

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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.

<ESMA_QUESTION_PRIIPs_42>
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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>
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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>
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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>
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46. Do you think this list is comprehensive? Should these different types of costs be further defined?

<ESMA_QUESTION_PRIIPs_46>
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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>
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<ESMA_QUESTION_PRIIPs_47>

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

14

<ESMA_QUESTION_PRIIPs_48>
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49. Do you think this list and breakdown is comprehensive?

<ESMA_QUESTION_PRIIPs_49>
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50. Should the methodology for the calculation of these costs be further specified? How?

<ESMA_QUESTION_PRIIPs_50>
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51. Should the methodology for the calculation of these costs be further specified? How?

<ESMA_QUESTION_PRIIPs_51>
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52. Should the methodology for the calculation of these costs be further specified?

<ESMA_QUESTION_PRIIPs_52>
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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>
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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>
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55. Should the methodology for the calculation of these costs be further specified?

<ESMA_QUESTION_PRIIPs_55>
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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>
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<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>
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<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>
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<ESMA_QUESTION_PRIIPs_58>

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

<ESMA_QUESTION_PRIIPs_59>
EUSIPA is of the opinion that for a given list of costs, the two approaches are similar. They essentially are only different ways of presenting the same result.

EUSIPA wishes it to be noted that the "fair value" is a theoretical value. It is a model price and should not be confused with an actual trade price. Manufacturer should, even if the "fair value" or "intrinsic value" of the product is used to determine the TCR, not be obliged to publish such value. The intrinsic value is not a trade price (not even professional market participants can purchase the product or the components of the product at such price). The "fair value" does not correspond to the amount used to provide/generate the return. Thus, the publication of the value would mislead investors as it depends on various variables (funding curves, internal accounting rules, market data). The value will differ considerably between manufacturers and would not add any sensible information for investors. <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>
EUSIPA does not see any specific cost for Structured Deposits whose pricing is done basically on same funding approach as for EMTNs. <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>
EUSIPA partially agrees.
The exhaustive list of costs should in our eyes be denominated as follows:
Distribution fees / expected transaction costs (which includes hedging costs)/ direct costs / capital costs / manufacturer costs / exit costs.

Generally, EUSIPA underlines that all costs known by the manufacturer or an amount corresponding to the manufacturers' estimate of such costs are embedded in the product price.

EUSIPA sees no benefit in splitting the total entry costs embedded in a product into the different components, since for most of the components the manufacturers are forced to operate with cost estimates, since the actual costs are not known on a single structured product basis. Accordingly, cost allocations to single components may change during the life time of the product resulting in a reduction of the manufacturer margin. If a separation of costs is imposed, it should consequently be limited to distribution fees and manufacturer fees.

Should we differentiate between "delta 1" and "option based" structured products?

EUSIPA sees no need to differentiate between "delta one" and option-based (bearing in mind that "delta" one is a particular case of an option).

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?

EUSIPA would outline the following cases where a manufacturer will not know all costs:
- When a product designed by the manufacturer is repackaged in another wrapper, the manufacturer will not know the fees linked to the final wrapper.
- When a fund is the underlying of a structured product, the manufacturer will not know costs linked to the fund. <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>
EUSIPA hints to the fact that above named costs have already been described in the list of "entry costs". In particular, the expected transaction costs (namely those for replicating the performance of the components) are included as an estimate in the entry costs. To clarify, transaction cost exceeding the estimate are ultimately borne by the manufacturer and not charged to the investors, which therefore do not represent a cost from the point of view of the investors and hence does not need to be disclosed in addition to already published costs.

The fact that costs can be paid on a running basis or upfront should not be a criterion to distinguish them in principle. Running fees that impact the product performance could be disclosed as ongoing charge only to the extent these running fees cannot be discounted to a present value. Usually for a model-evaluated product with fixed term running fees can be expressed as an upfront percentage, in which case we suggest including them also in upfront cost.
Only for products valued without use of models such as open-ended TIPP/CPPI, or an open-ended actively managed certificate usually a management fee and sometimes transaction costs are charged to the NAV of the product on an on-going basis and is not included in the issue price. In this case it would make sense to disclose these costs as on-going charges. <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>
EUSIPA underlines that by "proportional fees" we understand penalties for early exit expressed in % of the notional (e.g. for a product which has exit penalties such as 1% in year 1, 0.5% year 2, 0.25% in year 3 and nothing from and including year 4 until maturity. These should be disclosed in the cost section, but not double-counted in the total cost ratio (TCR) as they would only occur under specific circumstance.
EUSIPA wishes to stress that exit fees generally serve the purpose of protecting the sales commissions and structuring costs, which should be explained to investors.
Underlying however is the question of what basis should be used to calculate the spread ex ante (this could be nominal value or the net asset value).
Any exit spread indicated in the cost information of a KID could be a maximum spread only. <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>
EUSIPA refers to our answer to question 61 above.
<ESMA_QUESTION_PRIIPs_64>

65. Would you include other cost components?

<ESMA_QUESTION_PRIIPs_65>
No, EUSIPA would not include other costs components. <ESMA_QUESTION_PRIIPs_65>

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

<ESMA_QUESTION_PRIIPs_66>
EUSIPA is of the opinion that any costs of the underlying (e.g. index licence cost) is a cost borne by the manufacturer, which is implicitly included in the direct costs and priced upfront already. It should hence not be included in on-going costs. <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>
EUSIPA does not foresee any issue with the amortization of entry cost.
Should the ESAs believe amortization to lead to issues with the clients, examples are welcome along with guidelines to deal with such issues.
The term invested capital is misleading. "Notional invested" or "Denomination" are in our view the correct legal terms which should be used. The payoff of the SP applies on the notional invested, which may be different from the purchase ("investment") price times notional.
For products sold "in units" (i.e. without a denomination such as Call paying absolute difference between Spot and Strike), a hypothetical denomination could be set to the strike level, so that the payoff is expressed in percentage of the strike.
As long as the denomination of the security (or notional invested for a structured deposit) is clearly displayed on the KID, we do not foresee any regulatory issues. <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>
EUSIPA does not see such issues. All estimated transaction costs are priced upfront. As stated before, late adjustments would not be passed on to the investor. <ESMA_QUESTION_PRIIPs_68>

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

<ESMA_QUESTION_PRIIPs_69>
EUSIPA takes the view that pricing models to determine costs should not be prescriptive. <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>
EUSIPA is of the opinion that as far as costs are specifically concerned, we do not believe that there should be a need for an update.
For example, as for transaction costs, while the assessment of their initial level is a key component of the initial determination of the product price, their actual realisation is without impact to the cost charged to the investor or to the product price on the secondary market.
EUSIPA upholds that for structured products, in contrast to funds, the profit or loss incurred by the manufacturer in connection with the hedging-trading activity that follows the sale of the product is without impact to the investor as concerns the value of his investment. <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>
EUSIPA would like to reiterate that, as was expressed earlier manufacturer-internal models represent the best approach as they respond best to the relevant (offered) product landscape.
Furthermore, as pricing models rely on the assumption that the risk premium is set at zero (risk neutral environment), there is no need for a prescriptive approach either. <ESMA_QUESTION_PRIIPs_71>

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

<ESMA_QUESTION_PRIIPs_72>
EUSIPA is not aware of such. <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>
EUSIPA reiterates that the industry has a long experience of using forward looking models based on a well-developed theoretical basis. Although they are useful to calibrate model parameters, backward looking models cannot be used for valuation purposes as they do not provide a full valuation model given that past data do not provide an adequate view on the future evolution of the underlying. <ESMA_QUESTION_PRIIPs_73>

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

<ESMA_QUESTION_PRIIPs_74>
In the eyes of EUSIPA, the swap rate curve appears to be the best reference as it represents an established global industry benchmark. For exotic currencies however, the manufacturer should have the possibility to define an appropriate different reference. <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>
EUSIPA does not believe that other market data should be used to determine the credit risk as it is already implicitly included in the funding spread curve. <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>
EUSIPA wishes to stress that the absence of observable market data does not prevent the manufacturer from valuating a product as long as the funding spread is known (the credit risk is implicitly included in the funding spread). <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>
EUSIPA wishes to outline that the cost-wise appreciation of counterparty risk will depend on the margining scheme in place among the concerned counterparties (i.e. bilateral or multilateral). CVA models are market practice. Though each institution has its own model, each generally relies on common theoretical assumptions. CVA is generally split into two main components: default probability and loss in case of default. <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>
To the understanding of EUSIPA the partial un-observability of parameters is not a novelty in finance. To some extent, it may even be argued that the very reason for developing models is the need to be able to convert discrete observations of parameters (or their proxies) into a continuous model. In other words, financial institutions are used to cope with situations where some parameters may not be observed/observable. Whilst EUSIPA does not believe that it would be possible to list all situations where this un-observability may occur, we note that these situations do not create a detriment to investors and are hence without impact to the cost structure.
- As an example, in case of a hedging disruption (meaning the manufacturer is not in a position to acquire the hedge anymore), a valuation may still be determined. Such situations are also described in the base prospectus and relevant ISDA event definitions. <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>
EUSIPA upholds the view that it is not possible to prescribe a model that would give reliable prices for a decent proportion of structured products. Instead it should be much more effective to rely on internal models, which are audited by prudential regulators. <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>
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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>

NA (as relevant for funds only) <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>
EUSIPA believes that the relevant figure for an "initial invested amount" should be:

- The denomination for securities,
- An hypothetical denomination set to the Strike level for products "in units", and
- The notional for structured deposits.

An amount of 1000 EUR (or local currency equivalent in non-Euro countries) seems a reasonable assumption for the initial invested amount (for denomination or notional). For securities settled in units, this initial investment should be understood as being the strike (or initial spot price), depending on the market convention. <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>
NA (not relevant for structured products) <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>
EUSIPA basically agrees with the considerations. We do not see a particular difficulty in the annualization of costs. Cost should be annualized on the maturity/term of the product and, for open ended products, based on the recommended holding period, which we propose to assume with 10 years. <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>
EUSIPA would stress that for structured products the most simple way is to amortize linearly entry and exit costs over the recommended holding period. <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>
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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>
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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>
EUSIPA wishes to underline that once the aggregate costs of the structured product are determined, it is a straightforward exercise to annualize them. The question that could be raised here seems to be more about the different ways to measure costs.
We think the "average net investment" or the "investment" is misleading and not a relevant concept for structured products. As explained in question 82, it should be denomination (for securities) or notional (for deposits).
EUSIPA does see an issue however with expressing the cost as a percentage of the average net investment value. The reason for this is that if the product "mark to market" increases (e.g. to EUR 1000 * 120%, = EUR 1200), while a notional of EUR 1000 is invested, the cost for the structured product remains usually a fixed percentage of the notional and not of the average net investment value. In addition, the average net investment value cannot be known at trade date. As stated before, the TCR for structured products should therefore be a percentage of a denomination or notional. <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>
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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>
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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>
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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>
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93. Do you identify any specific issue in relation to the implementation of the RIY approach to funds?

<ESMA_QUESTION_PRIIPs_93>
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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>

Generally EUSIPA would like to stress that for structured products, the underlying assumption of the "Reduction in Yield" ("RiY") approach (that assimilates all costs with a loss of opportunity) does not represent the appropriate choice to properly establish and communicate product costs.

Main reason is that for structured products, the "RiY" approach generally implies that the product may be assembled by a mere assimilation of a zero coupon and a vanilla derivative. While this (frequently-held) view may be true in a static approach, it is untrue under a realistic market perspective.

In reality, a structured product manufacturer is not a mere custodian of two basic components. To the contrary the manufacturer plays a dynamic hedging role over the entire lifespan of the product. This hedging activity will permit to constantly adapt the derivative coverage/exposure of the product, in order to ensure that it delivers the contractual formula agreed for the said product.
The described hedging function is hence an intrinsic element of the value of any structured product.

To the strong conviction of EUSIPA the related cost must therefore consequently be approached under an added-value logic and not a as "loss of opportunity" for the investor, as presented in this section and assumed under the "RiY" approach. <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>
EUSIPA takes the view that for structured products, returns should be calculated on the Denomination amount (e.g. EUR 1000 or equivalent in local currency) which means net of implicit Entry costs. Regarding the growth rate on the invested amount to estimate cumulative effect of costs, a zero growth rate seems appropriate for structured products. This simply means the Denomination (used as the basis to express cost as a % of Denomination) remains unchanged throughout the life of the product. <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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<ESMA_QUESTION_PRIIPs_96>

97. What costs impact the return paid on the products?

<ESMA_QUESTION_PRIIPs_97>
EUSIPA is of the view that SPVs should be treated in the same way as structured products, please refer to question 61. <ESMA_QUESTION_PRIIPs_97>

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

<ESMA_QUESTION_PRIIPs_98>
EUSIPA does not see any difficulties. The TCR concept is applicable to EMTNs, as well as to SPVs. <ESMA_QUESTION_PRIIPs_98>

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

<ESMA_QUESTION_PRIIPs_99>
As stated earlier, EUSIPA is of the opinion that the RIY concept is not suitable for Structured Products or Funds. <ESMA_QUESTION_PRIIPs_99>