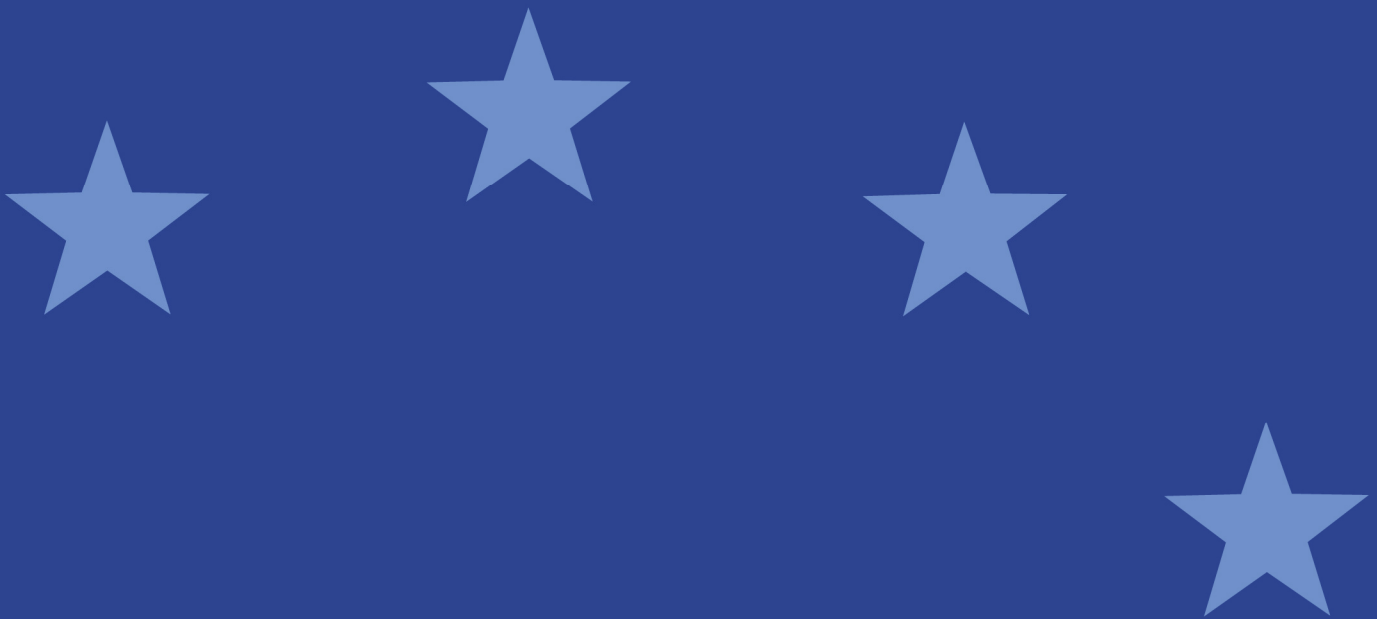




European Securities and
Markets Authority

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'.

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	Bund der Versicherten (BdV - German Association of Insured)
Activity	Non-financial counterparty
Are you representing an association?	<input checked="" type="checkbox"/>
Country/Region	Germany

Introduction

Please make your introductory comments below, if any:

< ESMA_COMMENT_PRIIPs_1 >

As Germany's most important NGO of consumer protection related to private insurances (with more than 50.000 individual members) we would like to thank the European Supervisory Authorities for the opportunity to publish comments on this consultation. For our comments we selected questions with a general issue or related to insurance-based investment products.

< 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>

Yes, we fully agree upon the three main elements of the risk-reward-profile outlined on page 8 of the DP. We prefer a stochastic modelling based on parameters estimated from historical data, which should be combined with parameters estimated from current market prices of derivatives and other forward looking contracts (approaches b and c; DP, p. 10). In order to ensure a consistent approach, "historical" data should be added. A good example is the data of long-term development of guaranteed interest rates and of surplus participations related to "classical" German life insurances. Of course the current on-going situation of low interest rates has to be taken into account. Additionally back-tests should regularly be published by the insurers.<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>

Related to insurance-based investment products the most important "risk" for consumers are costs. Costs reduce the amount actually invested (investment part of premium) from the very beginning of the contract, consequently even with an excellent "intrinsic performance" of the chosen PRIIP the maturity value will considerably be reduced at the end of the product life-cycle (by effect of compound interest). That is why disclosure of costs and a probabilistic presentation of possible returns are essential.

Related to pure investment products a recommendation of a risk measure for each PRIIP category by EIOPA should be given. If a manufacturer uses a non-appropriate risk measure, EIOPA should use its product intervention powers.

Additionally we would like to emphasize that related to private pension products or long-term retirement saving plans in July 2015 the Fraunhofer Institute for Industrial Mathematics (directed by Professor Ralf Korn, University of Kaiserslautern) has been given a new responsibility. It will fulfill its new function as Product Information Centre for Pensions (PiA) in Germany. The role of the PiA is to simulate the performance of State subsidized pension plans and rate them in terms of risks and opportunities. So we strongly recommend to take into consideration the research work and the practical experiences by this Fraunhofer Institute, in order to choose the model parameters for the purposes of calculating a risk measure by the future regulatory technical standards. The PiA has to establish the technique of calculating an accumulated cost-measure as well.

New provisions related to risk-reward-classes and to the disclosure of costs, which shall be used for "product information sheets" of state-subsidized pension plans, were recently adopted by the German legislator (cf. "Altersvorsorge-Produktinformationsblattverordnung" – AltvPIBv - articles 5 and 7, in: Bundesgesetzblatt, Jahrgang 2015, Teil I, Nr. 32 am 31. Juli 2015).

<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>

For insurance-based investment products the benchmark should be the amount invested grown at the rate of inflation (option c, DP p. 13). The various with-profits-mechanisms entail the participation at the development of interest rates and/or inflation.

<ESMA_QUESTION_PRIIPs_3>

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

<ESMA_QUESTION_PRIIPs_4>

Yes, we fully agree that implicit or explicit growth rates should be assumed for purpose of estimating total aggregate costs. Only this assumption allows comparisons between different types of PRIIPs and will be able to prevent from any kind of misleading information for consumers. Therefore we choose option b (cf. DP p.14): “The asset grows at the risk free rate adjusted for an asset specific risk premiums (with the hypothesis that the risk premium is different from zero and constant).”

We would like to emphasize that related to private pension products and long-term retirement saving plans in Germany recently the Fraunhofer Institute for Industrial Mathematics (Kaiserslautern) has been given a new responsibility. It will now also function as Product Information Centre for Pensions (PiA). The role of the PiA is to simulate the performance of State subsidized pension plans and rate them in terms of risks and opportunities. This includes possible growth rates. So we strongly recommend to take into consideration the research work and the practical experiences by this Fraunhofer Institute, in order to choose the model parameters for the purposes of calculating a risk measure by the future regulatory technical standards.

<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>

Related to insurance products the appropriate time frame depends on the duration of the contract, i.e. 12, 20, 30, 50 and even more years for life insurances and annuities, for not only the investment / contribution phase, but also the pay-out phase has to be taken into account..<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>

TYPE YOUR TEXT HERE

<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>

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<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>

TYPE YOUR TEXT HERE

<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>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_PRIIPs_9>

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

<ESMA_QUESTION_PRIIPs_10>
TYPE YOUR TEXT HERE
<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>
TYPE YOUR TEXT HERE
<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>
TYPE YOUR TEXT HERE
<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>
TYPE YOUR TEXT HERE
<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>
TYPE YOUR TEXT HERE
<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>

Performance scenarios should always be based on probabilistic modeling. We would like to emphasize that the recently established Product Information Centre for Pensions (PiA) at the Fraunhofer Institute for Industrial Mathematics (Kaiserslautern) chose the probabilistic approach, because any what-if-approach can be manipulated too easily (cf. our comments on Q 2 and Q4). Therefore we fully agree upon the statements on what-if approaches outlined in the DP (p. 47). If the choice is left to the manufacturer, "... there is no guarantee that the picture it provides of the product is accurate or realistic, as it depends on the choices of the manufacturer. This approach is relatively easy to manipulate and comparability is low because manufacturers can choose different scenarios." If there is a

pre-scribed approach, "...there is a risk of manufacturers designing their product to optimize presentation given the predefined scenarios that may introduce distortions in the market."
<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>

No, we do not think that these principles are sufficient to avoid the risks of manufacturers presenting a non-realistic performance picture of the product. So these principles should be reinforced. Even if the probabilistic model is chosen, manufacturers will be able to align their product developments on these parameters. NCAs will have to revise the product innovations under this particular performance picture, too.
<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>

Cf. our comment on Q15.<ESMA_QUESTION_PRIIPs_17>

18. Which percentiles do you think should be set?

<ESMA_QUESTION_PRIIPs_18>

We propose the 25th percentile as pessimistic, the 50th percentile as neutral and the 75th as optimistic approach.

<ESMA_QUESTION_PRIIPs_18>

19. Do you have any views on possible combinations?

<ESMA_QUESTION_PRIIPs_19>

Options a) and b) are very interesting, but relevant only from a theoretical perspective. For the consumers the results of any probability approach have to be intelligible, that is why we prefer option c).

<ESMA_QUESTION_PRIIPs_19>

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

<ESMA_QUESTION_PRIIPs_20>

No, credit events should not be considered in the performance scenarios. The individual circumstances will differ too strongly (amount, interest rate, duration, etc.). If you include credit events, then biometric events could be included as well (e.g. high mortality because of an epidemic or very low mortality because of a breakthrough in the treatment of cancer). But this would make the approach much too complicate.

<ESMA_QUESTION_PRIIPs_20>

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

<ESMA_QUESTION_PRIIPs_21>

If the PRIIP is a life or annuity insurance, redemption events must be considered. In Germany there are more than 80 million contracts of capital life insurances and annuities, which almost all are calculated according to the zillmerisation method. That is the reason, why entry or acquisition fees (as costs category)

have to be included as well as biometric costs of life annuities. The early redemption costs are already included. They are particularly important, because more than 60% of life insurance contracts are cancelled before reaching maturity.

<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>

Cf. our comment on Q 21.

<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>

TYPE YOUR TEXT HERE

<ESMA_QUESTION_PRIIPs_23>

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

<ESMA_QUESTION_PRIIPs_24>

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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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<ESMA_QUESTION_PRIIPs_26>

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

<ESMA_QUESTION_PRIIPs_27>



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<ESMA_QUESTION_PRIIPs_27>

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

<ESMA_QUESTION_PRIIPs_28>
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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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<ESMA_QUESTION_PRIIPs_31>

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

<ESMA_QUESTION_PRIIPs_32>
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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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<ESMA_QUESTION_PRIIPs_33>

34. Is this description comprehensive?

<ESMA_QUESTION_PRIIPs_34>
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<ESMA_QUESTION_PRIIPs_34>

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

<ESMA_QUESTION_PRIIPs_35>
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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 (booking fees paid to custody banks that are billed separately from the annual custodian fee paid for depositing the securities) should be added to this list?

<ESMA_QUESTION_PRIIPs_36>
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<ESMA_QUESTION_PRIIPs_36>

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

<ESMA_QUESTION_PRIIPs_37>
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<ESMA_QUESTION_PRIIPs_37>

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

<ESMA_QUESTION_PRIIPs_38>
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<ESMA_QUESTION_PRIIPs_38>

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

<ESMA_QUESTION_PRIIPs_39>
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<ESMA_QUESTION_PRIIPs_39>

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.

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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<ESMA_QUESTION_PRIIPs_40>

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

<ESMA_QUESTION_PRIIPs_41>
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<ESMA_QUESTION_PRIIPs_41>

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

<ESMA_QUESTION_PRIIPs_42>
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<ESMA_QUESTION_PRIIPs_42>

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

<ESMA_QUESTION_PRIIPs_43>
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<ESMA_QUESTION_PRIIPs_43>

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

<ESMA_QUESTION_PRIIPs_44>
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<ESMA_QUESTION_PRIIPs_44>

45. Which of the above mentioned options 1 and 2 for the calculation of aggregate costs would you prefer? Do you agree with above mentioned assumptions on the specificities of the costs of life-insurance products? How should the breakdown of costs showing costs specific to the insurance cover be specified? Do you think that risk-type riders (e.g. term or disability or accident insurances) have to be disregarded in the calculation of the aggregated cost indicator? How shall risk-type rider be defined in this context? (one possible approach might be: A risk-type rider in this context is an additional insurance cover without a savings element, which has separate contractual terms and separate premiums and that the customer is not obliged to buy as a compulsory part of the product).

<ESMA_QUESTION_PRIIPs_45>

We prefer option 1, and we agree with the assumptions outlined on the specificities of the costs of life-insurance products. Additionally to ongoing costs of administration and of capital investment (as for pure saving products), insurance products include biometric costs. This special feature does not only represent costs, but may be a source for additional benefits for the insurers, too (depending on the more or less “prudential” calculation of life expectancy). That is reason, why these costs have to be disclosed aiming at a level-playing field amongst all categories of PRIIPs.

Risk-type riders (e.g. term or disability or accident insurances) should be disregarded in the calculation of the aggregated cost indicator, because the individual circumstances will differ too strongly (insured sums, percentages, duration, loading for pre-existing illness etc.). In contrast to “fair value” (for structured products) and to “total expense ratio” (for open-ended funds), “reduction in yield” (RiY) might be used for preparing “total aggregate cost” figures. But why should RiY be used for investment funds, if there is already a common calculation method of costs? RiY itself has to be seen in a very critical way: costs are calculated in relation to yields or returns, which are only probable, but the costs are always fixed. Additionally RiY strongly depends on the duration of the accumulation phase. The shorter it is, the more expensive the contract seems to be. Therefore various offers that differ in the duration of the accumulation phase cannot be compared at all via the RiY. Last but not least: RiY is only valid, if the contract is not cancelled before reaching maturity.

Therefore we propose as alternative and transparent reference parameter for costs “Reduction in Wealth” (RiW). This parameter was presented by the ZEW-Zentrum für Europäische Wirtschaftsforschung Mannheim (Centre of European Economic Research) in 2010 for the German Federal Ministry of Finance in its final report on transparency of state-subsidized retirement products (Abschlussbericht Nr. 7/09: Transparenz von privaten Riester- und Basisrentenprodukten). This parameter compares the real maturity value reduced by the sum of all types of costs occurring during the life-cycle of a product and the hypothetical maturity value of any retirement products without any reduction of investments and of pay-outs by costs. The difference between the two maturity values is given by a percentage (for more information about the “Reduction in Wealth”, cf. our comment on Q 87).

<ESMA_QUESTION_PRIIPs_45>

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

<ESMA_QUESTION_PRIIPs_46>

Yes, we agree upon this list (cf. structure of costs following to the German law of product certification of retirement provision contracts 2001, amended 1 April 2015: Altersvorsorgeverträge-Zertifizierungsgesetz (AltZertG), article 2a: Kostenstruktur). Nevertheless we propose adding these factors to the key questions: one-off/single acquisition costs and ongoing administrative costs.

The “classical” capital life insurance contracts in Germany (more than 80 million contracts) are calculated by the zillmerisation method, therefore the entry fees are particularly high. Following to German law these costs have always to be presented by absolute monetary amounts. Additionally the ongoing development of surrender values should be presented.

<ESMA_QUESTION_PRIIPs_46>

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

<ESMA_QUESTION_PRIIPs_47>

We agree upon the solution that several numbers of surrender events should be shown. We would like to underline that the “costs for biometrical costs” are not easily to depict, especially for longevity. But within the concept of “Reduction in Wealth” the costs of longevity can be included like all the other cost parameters if explicitly disclosed or not (cf. our comment on Q 87).

<ESMA_QUESTION_PRIIPs_47>

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

<ESMA_QUESTION_PRIIPs_48>

Yes, the methodology for the calculation of the aforementioned costs should be specified related to the reduction in wealth. Costs reduce the amount actually invested (investment part of premium) from the very beginning of the contract, consequently even with an excellent “intrinsic performance” of the chosen PRIIP the maturity value will considerably be reduced at the end of the product life-cycle (by effect of compound interest). In new categories of PRIIPs the maturity value may additionally be reduced by performance fees.

<ESMA_QUESTION_PRIIPs_48>

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

<ESMA_QUESTION_PRIIPs_49>

Yes, we think this list and breakdown is almost comprehensive. During the decumulation / pay-out phase there are additional ongoing administrative costs for the payment of the annuities, which again reduce the pay-outs.

It must be underlined that this profit sharing between insurance company and policy holder is favorable to the former. At least in Germany following to the law, only 50% of cost benefits have to be reimbursed to the policy holders (and 90% of risk benefits). But these minimum regulations may be better as if there is no regulation at all.

<ESMA_QUESTION_PRIIPs_49>

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

<ESMA_QUESTION_PRIIPs_50>

The reference parameter for costs should be clarified in relation to the “reduction in wealth” (cf. our comment on Q 87). By using the calculation method of “reduction in wealth” all types of costs (eg. costs of the biometric risk of longevity) and the different types of profit sharing (eg. resulting from risk benefits) can be included.

<ESMA_QUESTION_PRIIPs_50>

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

<ESMA_QUESTION_PRIIPs_51>

Cf. our comment on Q 50. Example: in Germany sometimes the costs of guarantees are explicitly disclosed (cf. the pension product “ERGO Garantie”), but mostly they are hidden. If “reduction in yield” is used as the calculation methodology in this case, the former manufacturer is even discriminated to the latter. In order to avoid such a discrimination, we clearly propose the calculation methodology of “reduction in wealth”, which includes all types of costs notwithstanding disclosed or hidden (cf. our comment on Q 45).

<ESMA_QUESTION_PRIIPs_51>

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

<ESMA_QUESTION_PRIIPs_52>

First we would like to emphasize that we consider “penalty fees” as being wrong in themselves. A consumer has the right to cancel a contract whenever he wants (because the payments or contributions are his money!), and he must not be “punished” for his possible wish of redemption.

We do not think that the possibility of early surrender is similar to an American put option, because life insurers calculate these possible costs in advance. The methodology of calculation of these costs will have to be further specified related to the way how they are disclosed.

Example: the “classical” capital life insurance contracts in Germany (more than 80 million contracts) are calculated by the zillmerisation method. But the zillmerisation method takes into account only the entry

fees, any possible “penalty fees” for early redemption have to be added. Therefore the surrender values are very low during the first years of the contracts.

We propose as the only transparent way in order to disclose the long-term effects of accumulated entry fees and early redemption fees: there has to be added a list of surrender values for each year of the entire duration of the contract as part of pre-contractual information obligations. German life insurers usually add such a list.

<ESMA_QUESTION_PRIIPs_52>

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

<ESMA_QUESTION_PRIIPs_53>

Yes, fund related costs also exist for with profit life insurance products (with the accumulated capital assuming the role of the fund). In general we think that the differences amongst the different types of life insurance blur, because they become more and more complex related to their capital investments or asset allocations. But the presentation of these products for the consumers still follows apparently clear product classifications (classical, with-profit, unit-linked, hybrid etc.). This may entail even a misleading information for the consumers.

That is the reason why we urge that the entire regime of cost disclosure has to be completely independent from any type of particular product and its specific options for capital investments.

<ESMA_QUESTION_PRIIPs_53>

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

<ESMA_QUESTION_PRIIPs_54>

Related to insurance products, all varieties of investment fees, including performance fees, should be disclosed as a percentage of the reduction in wealth. The examples of these costs are not only found in unit-linked products, but in classical life insurances and other types of PRIIPs as well (cf. comment on Q 45 and Q 53).

<ESMA_QUESTION_PRIIPs_54>

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

<ESMA_QUESTION_PRIIPs_55>

Cf. our comment on Q 54.

<ESMA_QUESTION_PRIIPs_55>

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

<ESMA_QUESTION_PRIIPs_56>

All those costs related to profit sharing could be included, if the insurers use the method of “Reduction in Wealth”. But this method - or any other method which we know hitherto - does not allow to distinguish between all types of costs. But even if there are a comprehensive list of all costs and a methodology disclosing them, future product innovations will always make them obsolete.

<ESMA_QUESTION_PRIIPs_56>

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

<ESMA_QUESTION_PRIIPs_57>

No, we do not agree. These types of costs can be found in non-with-profit-products as well.

<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>

In new categories of unit-linked PRIIPs or in PRIIPs with other “new” guarantees which are not linked to an ongoing minimum interest rate, performance fees for investment part of the premiums are a new phenomenon. That is why we propose to add performance fees to the types of costs. But even if there are a comprehensive list of all costs and a methodology disclosing them, future product innovations will always make them obsolete.

<ESMA_QUESTION_PRIIPs_58>

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

<ESMA_QUESTION_PRIIPs_59>

TYPE YOUR TEXT HERE

<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>

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<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>

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<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>

TYPE YOUR TEXT HERE

<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>
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<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>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_PRIIPs_64>

65. Would you include other cost components?

<ESMA_QUESTION_PRIIPs_65>
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<ESMA_QUESTION_PRIIPs_65>

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

<ESMA_QUESTION_PRIIPs_66>
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<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>
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<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>
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<ESMA_QUESTION_PRIIPs_68>

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



<ESMA_QUESTION_PRIIPs_69>
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<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>
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<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>
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<ESMA_QUESTION_PRIIPs_71>

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

<ESMA_QUESTION_PRIIPs_72>
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<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>
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<ESMA_QUESTION_PRIIPs_73>

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

<ESMA_QUESTION_PRIIPs_74>
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<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>
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<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>



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<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>
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<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>
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<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>
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<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>
In the case of life-insurance products x should be 50, for the duration has to encompass the death of the policy holder. In the case of mergers and acquisitions there is the real danger that the knowledge of calculation methods for very old contracts might get lost in the insurers concerned.
<ESMA_QUESTION_PRIIPs_80>

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

<ESMA_QUESTION_PRIIPs_81>
Yes, the terms “rank pari passu” is so far related to shares and other types of securities and therefore should be adapted to insurance-based products. Consumers usually do not know these expert terms which require high level financial knowledge.
<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>

The impact of fixed costs should be neither overestimated nor underestimated. Related to retail investment products with on-going annual payments the relevant figure for the initial invested amount seems to be appropriate. Related to insurance-based products with a single contribution the reference parameter should be 10.000.

<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>

For all contracts the individually calculated costs have to be disclosed in the KID related to the individual age and to the individual amount of the premium. The KID will always have to be a KID with “individualized” figures which is a common fact for the insurance industry. If the figures disclosed in the KID will not be individualized, the information given by the KID may often be misleading.

<ESMA_QUESTION_PRIIPs_83>

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

<ESMA_QUESTION_PRIIPs_84>

We mostly agree with. We would like to point out that - by taking into consideration only the accumulation phase - the methodology of “Reduction in Wealth” leads to the same results as TCR. But the “Reduction in Wealth” takes into account the decumulation phase as well. That is the reason why we prefer RiW to TCR (cf. our comment on Q 87).

<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>

Cf. our comment on Q 87.

<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>
 Cf. our comment on Q 87.
 <ESMA_QUESTION_PRIIPs_86>

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

<ESMA_QUESTION_PRIIPs_87>

Instead of referring to the reduction in yield we assume to establish the “reduction-in -wealth” instead. The Reduction in wealth is the average decrease of the maturity value caused by costs. That means: Let MV be the expected maturity value, i.e. that value that is expected under the given parameters and costs for the individual contract which the KID should refer to. And let iMV be the “ideal maturity value”, i.e. that value that would be reached under the same circumstances, but with the assumption that there are no costs at all.

Then the difference
 iMV-MV

is that what the consumer loses because of the effect of the costs.

Then

$RiW = 1 - MV/iMV$

is the “Reduction in Wealth” the effect of costs, given as the decrease of the maturity value.

Simplicity of understanding: The “RiW” is very much simpler to understand than the “RiY”. For example if you inform an average consumer, “the costs have the effect that you will get 20% less, than you would get without costs”, then the consumer gets a better idea about the costs as if you would tell him, “because of the costs the average interest rate of your investment will be reduced by 1,1%”.

Simplicity of computing: From a technical point of view the computing of the RiW is as complicated as computing the RiY. In fact by a given RiY it is easy to compute the RiW and vice versa. Let GP_m be the gross premium in the m-th year of the contract, let n be the length of the accumulation phase (in years), let i be the interest rate without costs and let RiY be the Reduction in yield. Then you get the Reduction in Wealth RiW via:

$$RiW = \frac{\sum_{j=0}^{n-1} GP_j * (1 + i - RiY)^{n-j}}{\sum_{j=0}^{n-1} GP_j * (1 + i)^{n-j}}$$

Inclusion of costs of the decumulation phase: So far the RiW will take into account only the costs of the accumulation phase. But additionally the costs of the decumulation phase will be taken into account as well: Let AN be the expected annuity, i.e. that annuity that is calculated with the precise mortality table of the insurer taking into account all further costs occurring during the decumulation phase. And let iAN be the ideal annuity, i.e. that annuity that the consumer would get if he annualizes the ideal maturity value iMV with the mortality table without prudential assumptions.

Then the difference

$iAN-AN$

is that what the consumer loses as annuity because of the effect of the costs.

Then $RiW=1-AN/iAN$ is the "Reduction in Wealth" the effect of costs, given as the decrease of the annuity, now taking into account all costs, including those costs of the decumulation phase.

If you are more interested in the idea of RiW , we would be very happy to get the chance to explain more and in detail. The scientific literature which we know hitherto is published only in German:

ZEW-Zentrum für Europäische Wirtschaftsforschung Mannheim, Abschlussbericht Nr. 7/09: Transparenz von privaten Riester- und Basisrentenprodukten (cf. our comment on Q 45);

Axel Kleinlein: Die "Kostenquote der Versicherer" kann Verbraucher in die Irre führen, in: Versicherungswirtschaft, Heft 7 vom 1. April 2011, S. 457-460.

<ESMA_QUESTION_PRIIPs_87>

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

<ESMA_QUESTION_PRIIPs_88>

Cf. our comment on Q 87.

<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>

Cf. our comment on Q 87.

<ESMA_QUESTION_PRIIPs_89>

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

<ESMA_QUESTION_PRIIPs_90>

Cf. our comment on Q 87.

<ESMA_QUESTION_PRIIPs_90>

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

<ESMA_QUESTION_PRIIPs_91>

The main difference between on-going charges of funds and on-going charges of life-insurances is that the latter do not depend on the volatility of financial markets. As pointed out in the DP “the ongoing charges figure shall be calculated at least once a year, on an ex-post basis” (p. 102). “The ex-post figure shall be based on recent cost calculations which the management company has determined on reasonable grounds to be appropriate for that purpose” (p. 103). Cf. our comment on Q 87.

<ESMA_QUESTION_PRIIPs_91>

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

<ESMA_QUESTION_PRIIPs_92>

The cost of embedded options of life insurance products should be estimated following to “a rule for the profit sharing and a model of the early surrender of policyholder (all those rules and models being disclosed to the supervision authority under Solvency II framework)” (DP, p. 104). In the case of life-insurance contracts a breakdown on a per contract of future discretionary benefits has hitherto always been possible and constitutes an essential information for the customers.

<ESMA_QUESTION_PRIIPs_92>

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

<ESMA_QUESTION_PRIIPs_93>

If funds are “wrapped” by an insurance cover, i.e. they are part of a PRIIP, the approach of RiY is not appropriate, not intelligible and therefore mis-leading for consumers. (cf. our comments to Q 45 and Q 87).

<ESMA_QUESTION_PRIIPs_93>

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

<ESMA_QUESTION_PRIIPs_94>

If structured products are “wrapped” by an insurance cover, i.e. they are part of a PRIIP, the approach of RiY is not appropriate, not intelligible and therefore mis-leading for consumers. (cf. our comments to Q 45 and Q 87)

<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>

Reduction in Yield itself has to be seen in a very critical way: costs are calculated in relation to yields or returns, which are only probable, but the costs are always fixed. Additionally RiY strongly depends on the duration of the accumulation phase. The shorter it is, the more expensive the contract seems to be. Last but not least: RiY is only valid, if the contract is not cancelled before reaching maturity (cf. our comment to Q 45 and Q 87).

<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>

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<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>

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<ESMA_QUESTION_PRIIPs_98>

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

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