	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	**Deadline** **6 December 2018** **23:55 CET**
Name of Company:	Austrian Association of Investment Fund Management Companies (VOEIG)	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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Reference	**Comment**	
General Comments	We welcome the initiative to address the obvious shortcomings of the current PRIIP KID as the confusion of investors – particularly in relation to performance and costs - is one of the most important subjects to tackle in order to enable the document fulfil its purpose. The Commission's unilateral decision to defer the PRIIPs Regulation's review, originally required to be completed by the end of 2018, to an unforeseen future date, does not change the necessity of such a full-scale review to commence (and be completed) as early as possible to address the most pressing issues. We are therefore concerned by the ESAs' comment that the "*comprehensive review of the PRIIPs framework […] is expected to be completed in the coming years*"[1].	

[1] ESAs' consultation paper, p. 12

	For us it is hardly understandable how the ESAs' approach the consultation itself. It is not in the best interest of retail investors to support the Commission's intentions to "phase out" the UCITS KIID by the end of 2019, upending the original sequencing as set out in the PRIIPs Regulation, and therefore having to put in place "quick fixes" that need to be agreed by the European co-legislators, at the latest, in Q2 2019 – only weeks before a new European parliament is elected and a new European Commission constituted. Furthermore, stakeholders are only given four weeks to respond and are being told that there will be no further stakeholder consultation to test the ESAs' chosen solutions. More importantly though, no consumer testing is being planned to ensure that the proposed amendments will actually address the current shortcomings. The amendments suggested by the ESAs may solve some of the issues at hand, but could exacerbate others. However, the answer to this question will only reveal itself after a "live test" on retail investors, which is unacceptable in our view. This unreasonable haste has another very unfortunate side effect that will negatively affect the outcome of these discussions. Due to this very limited timeframe to draw up amendments (by Q1 2019), the ESAs have also decided not to collect evidence on all other issues currently outstanding with the PRIIP KID, but have limited their review to performance scenarios. While we have always agreed that this issue is of utmost importance, other topics such as costs disclosures (e.g. transaction costs calculation and overall cost disclosures towards clients) are equally important and need to be considered. VOEIG urges the ESAs to fix the well-publicised shortcomings as a matter of priority. That being said, the Commission's deferral of the review also creates another issue. While targeted changes to the Level-2 requirements may address some issues currently plaguing the PRIIP KID, other issues can be solved only through changes to the Level-1 Regulation, again underlining the need for a holistic review, as originally specified by the co-legislators. Given the very limited scope of this consultation, which fails to address all outstanding issues, as well as having the serious potential to create further confusion among retail investors with the unstructured and rushed "phasing out" of the UCITS KIID, we insist that the exemption for UCITS must be extended by the co-legislators in order to allow for a proper review by the European	

Commission to take place as quickly as possible.

Additionally, we must point out that the UCITS KIID, just as the PRIIPs KID, is made for the retail investor and was never meant for professional investors, which makes the idea of providing UCITS KIIDs only to professional investors after the expiry of the exemption period even more odd.

Apart from that it must be clear that it is operationally impossible to comprehensively implement any changes to the Delegated Regulation (EU) 2017/653 and/or the Level 1 PRIIPs Regulation – regardless of which part of the Regulations they may concern – on the technical (IT-) level until the end of 2019.

We also request the co-legislators to assume their responsibility for the final switch from UCITS KIID to PRIIPs KID to be properly solved in all the legal documents that are concerned. This demand can only be met by establishing a realistic time frame to check and correct, delete and review every single part that is concerned – including the inevitable legislative change of the UCITS Directive in this respect.

The approach to “mend” parts of the UCITS KIID Regulation (EU) 583/2010 into the PRIIPs legislation[2] is to be questioned and can only be properly qualified in a broad discussion with accordingly enough time, because in the consultation paper on hand we cannot recognize the conception of the possible practical presentation of the new contents within the PRIIPs KID, not to mention the latent problem of the lack of space in the 3-pages-document.

With this in mind, we consider this ESAs’ consultation and our subsequent comments as only a first preparatory step towards to the full review in the near future and under a newly to be defined timeline.

To be clear, our comments should not be seen as any sort of endorsement to address substantial issues with rushed quick-fixes, i.e. amendments to the PRIIPs Delegated Regulation and its Annexes. VOEIG reiterates that the process (of review, targeted amendments where necessary and subsequent roll-out of PRIIPs to UCITS) put in place by the co-legislators in the PRIIPs Regulation (PRIIPs Regulation Articles 32 & 33) must be followed in order to avoid regulatory

[2] Section 4.3. of the ESAs’ consultation paper

	failure. We deeply regret and are very disappointed that the ESAs have not yet picked up the most important issues related to (i) the methodology used to calculate transaction costs and (ii) how cost information is presented to investors as a reduction-in-yield figure. How can the ESAs justify that investors who invest via investment funds have different transaction cost structures respectively transaction cost disclosures than investors who invest directly in the same underlying assets held by investment funds? How can they justify that cost disclosures and especially transaction cost disclosures are not understandable and misleading investors? <u>III.1. Transaction cost methodology</u> When drafting the PRIIPs Regulation (and MiFID II) lawmakers decided to reconsider (i) what should be considered a cost and (ii) how it must be disclosed to clients on an ex-ante basis[3]. This was a fundamental change to the previous MiFID I/UCITS KIID approach[4]. This new "all costs" figure now includes the ex-ante disclosure of transaction costs (and performance fees). Transaction costs consist of "explicit" costs (such as broker commissions, transaction taxes, etc.) and "implicit" costs. While there is no disagreement over what constitutes explicit costs, it was never fully clear how to calculate this implicit cost element. The MiFID II Directive tried to provide further clarity by stating that "underlying market risks" (i.e. market movements) should not be	

[3] Specifically:
- PRIIPs Regulation Article 8(3)(f) – states that the costs associated with the investment comprising both direct and indirect costs must be disclosed, and
- MIFID Article 24(4)(c) – states that all costs and charges in connection with the investment service and the financial instrument (which are not caused by the occurrence of underlying market risk) must be disclosed.

[4] It is important to make clear that the UCITS KIID already provides an all-inclusive cost figure (called the "ongoing cost figure" or OCF) to clients. At the time of its inception and in line with the (at the time) applicable MiFID I regime, the European co-legislators consciously decided against the disclosure of costs that are hard to predict on an ex-ante basis (such as performance fees and transaction costs). The simple reason for their exclusion was that such costs are highly dependent on unknown future factors such as the performance of the fund and overall market conditions. Also, no standards existed to estimate such costs. Up until now fund investors were informed about these costs only on an ex-post basis through the fund's annual reports

considered a cost[5].

Ignoring this essential clarification, the ESAs designed a completely new and complex approach (in the course of the Level-2 implementation process) on how to estimate these implicit costs, the "arrival price" methodology[6]. In essence, the ESAs decided that when calculating transaction costs, market movements (also called "slippage" – i.e. the time between the order and its execution) should also be considered a cost and should be added to the market spread. Therefore, any movement of the market between the time of the order and the time of the execution is to be considered a "cost" to clients. The PRIIP KID therefore equates such implicit costs that mostly capture a measure of the best-execution of a trade as an explicit cost to investors and equate them to all other types of costs (such as management fees) incurred by investors.

This methodology results in consistently under- or overestimating transaction costs. The first is particularly relevant if the fund manager executes trades in opposing moving markets (i.e. sells in an upward market and vice versa). This behaviour automatically results in negative transaction costs which is a highly misleading information. Thus, funds displaying overall negative transaction costs (see example below) are therefore simply the most visible outliers of this systemic flaw, but one must consider that incorrect costs are captured for each single transaction being recorded.

This exposes another flaw of the arrival price methodology, as it also assumes that the same high level of transparency (i.e. availability of price data) inherent in some liquid equity markets for all other financial markets. This is not the case. Due to the less transparent nature of trading in, for example, the bond markets or less liquid markets it is much more difficult to uncover the necessary arrival prices. It is instrumental to note that this issue of insufficient transparency in the non-equity markets is already being addressed by MiFID II and MiFIR through extensive changes to the EU's market structures, but these changes have only become (partly) applicable from 03 January 2018 onwards and will take years to take effect in order to arrive at the envisioned transparency regime.

In the meantime, information needed for the PRIIPs transaction cost calculation is either not

[5] MIFID Article 24(4)(c). Compounding this issue is that despite MiFID rules referring to costs "not caused by the occurrence of underlying market risk" ESMA's Q&As state that firms may comply with MiFID requirements by using PRIIPs cost methodology which includes market risk. So not only may figures not be comparable due to the different data points used by different managers under PRIIPs rules, some figures may be different as firms capture only the market spread and not "slippage" while following the MiFID Level-1 rules.

[6] To be precise, this model has been developed for funds operating for more than three years. An intermediate methodology called "new PRIIPs" exists for funds which operate for less than three years.

| | available, inappropriate or very hard and expensive to come by. The very theoretical and analytical nature of the methodology requires the development of extensive operational procedures and controls that result in extensive cost for all fund managers which are especially hard to bear for smaller companies that cannot leverage on larger economies of scale. As can be seen from our examples below, these costs are not proportional to the very limited added value of the information for the end investors, when other methods can provide more realistic cost estimates for much less money.

Overall, we think that the current “arrival price” methodology is not fit for purpose – due to the impact of market movements in the overall cost figure – and it is not providing fair, clear and non-misleading information to retail investors.

Also the current fall-back solution of “arrival price” methodology using same day opening or previous day closing prices is not leading to reliable results due to the significant bias by the market movement on a trading day. Therefore a complementary solution should be put in place that allows averaging of price data in the absence of reliable intraday prices. It is essential for less liquid, OTC or other asset classes for which the ‘arrival price’ methodology does not produce sufficiently accurate results.

This complementary solution could be based on the already existing “new PRIIPs” methodology. In essence, the revised method would be based on average observations of half the bid-ask spreads in certain assets/asset classes, which would then be multiplied by the actual fund turnover in the relevant asset class. This approach would also facilitate standardised observations of bid-ask spreads by way of spread tables.

<u>Redefine transaction cost calculation for real assets</u>

Real estate and other real assets such as infrastructure investments are currently treated as “other assets” for the purpose of transaction cost calculation. They are also subject to the “arrival price” methodology with the peculiarity that arrival price is calculated as “*the previous independent valuation price of the asset, adjusted for market movements, where appropriate, using an* | |

appropriate benchmark index"[7].

This provision does not account for the market realities. The price of e.g. real estate is subject to bilateral negotiations between the buyer and the seller and is neither assessable against any kind of price index. More importantly, the price or valuation of the asset itself is not in any way relevant for transaction cost calculations, since there are no implicit costs hidden in the price. All costs associated with transactions in real assets are being explicitly charged and thus, are fully known by the fund and already disclosed in the fund's annual report. They include in particular notary and brokerage fees and taxes for real estate transfer. Thus, costs of transactions in real assets should be calculated by summing identifiable cost items directly associated with a transaction.

III.2. Costs on Reduction-in-Yield basis are too difficult to understand for retail investors

The concept of the RIY (reduction-in-yield) currently being employed to disclose product costs towards retail investor is too complex. The fact that the costs include a time horizon and a yield represents a new type of theoretic disclosure that clients have not been familiar to date. Its complexity risks that it is easily misunderstood.

While we understand the reasoning and the (theoretical) added value of the RIY concept, we think we should also give cost disclosure the retail investors are more familiar with. We think that both disclosures can be given via the two cost tables currently required in the PRIIP KID.

The costs currently disclosed are purely theoretical, consumers should also be given the opportunity to see a product's costs without any theoretical assumption.

Table 1 (current cost disclosure exclusively using RIY)

Impact on return (RIY) per year	2.02 %	1.50 %	1.33 %

Table 2 (current cost disclosure exclusively using RIY)

[7] Cf para. 19 (a) (i) and (b) (i) of the Delegated Regulation's Annex VI.

This table shows the impact on return per year			
One-off costs	Entry costs	0.34 %	The impact of the costs you pay when entering your investment. This is the mos you will pay, and you could pay less.
Ongoing costs	Portfolio transaction costs	-0.04 %	The impact of the costs of us buying and selling underlying investments for the Fund.
	Other ongoing costs	1.03 %	The impact of the costs that we take each year for managing your investments.

1. The investor may believe that his entry costs are 0.34% while in reality he will pay 1% ; 0.34% correspond to 1% amortized over 3 years in case he stays invested for 3 years.

2. The investor may believe that he will pay 1.03% per year while this 1.03% is based on an assumption that the product will have a return of 2.65% per year and that the investor will hold the product for 3 years; the real ongoing costs will of course be different (and maybe radically different). Besides, the comparability with another investment is highly doubtful.

Q1

We generally agree that information on past performance should be included in the PRIIPs KID, where it is available. We believe that this is in line with the current wording of the Level-1 Regulation which does not explicitly forbid past performance to be disclosed alongside future performance scenarios.

While inclusion of past performance represents a short-term fix, we maintain that the

	accompanying future performance scenarios are not suitable for linear products, such as non-structured UCITS and AIFs[8], especially when such scenarios are derived from past performance data. For this very reason the UCITS KIID (which shows past performance data) is required to display a prominent warning about the relevance of past performance highlighting that it is not a reliable indicator of future results. Past performance should be the only performance indicator for linear products (in line with the current UCITS KIID framework). We would therefore suggest changes to the Level-1 Regulation to explicitly implement this recommendation in the PRIIP KID. That being said, we see very substantial practical problems with introduction of past performance into the current KID framework. If – as is being suggested by the ESAs – the past performance disclosures follow the current UCITS KIID rules, the past performance disclosure would take up approximately ½ A4 page. This is confirmed by the ESAs' own consultation in which the example on page 17 takes up half a page. Given the already dense information being provided and, more importantly, the Level-1 requirement to limit the PRIIP KID to three A4 pages, we do not see how this information can be included without seriously impeding the overall legibility of the PRIIP KID. We therefore suggest that the inclusion of past performance should be accompanied with potential changes to the Level-1 Regulation and the PRIIP KID's length to properly implement this in the PRIIP KID.	
Q2	It must be noted that structured UCITS are currently not required to include the past performance section. We believe that this should also be the case for structured UCITS and AIFs when producing a PRIIP KID. We understand that there may be substantial challenges for certain types of non-fund PRIIPs to include past performance information. Therefore, we would expect the ESAs to come up with a robust framework to ensure overall comparability between the information laid out to retail investors for all types of PRIIPs.	
Q3	If information on past performance is to be included in the PRIIP KID, we once again underline that	

[8] We acknowledge that structured products, such as structured UCITS and in line with the UCITS KIID requirements, foresee performance scenarios that can provide beneficial information about the developments of such product in different market scenarios.

	this information should be based on the UCITS KIID framework. This information is highly standardised and has been in use for more than seven years now, allowing retail investors to understand the nature of the disclosure. We need to point out that the chosen example for the presentation of past performance by displaying the use of a benchmark is not the common case. We would prefer an example without any benchmark, as this element has no impact on the subject and thus is neither important nor necessary - on the contrary, the current presentation may even cause misunderstandings and lead to an inadvertent outcome.	
Q4	From our point of view, simulations of any kind should basically be avoided – not least according to the beforementioned MiFID aspects. We understand the complexity of these discussions and again strongly underline that such decisions should be based on proper consultation with all stakeholders and the results confirmed by consumer testing. For this reason, we believe that such a question should be tackled in the full review of the PRIIPs Regulation rather than in this time-constrained exercise.	
Q5	The UCITS KIID framework already provides appropriate considerations for the use of simulated past performance. This is laid out in Article 19 of the UCITS KIID Regulation (Commission Regulation (EU) No 583/2010). We would assume that these principles could be applied to all types of PRIIPs. In addition, any simulated past performance information must be in line with MiFID II's Delegated Regulation 2017/565 Article 44 which provides the framework for "fair, clear and not misleading information requirements" in a MiFID distribution context.	
Q6	Yes, we consider the amendments to be a move in the right direction. However, this again leads to the problem of the lack of space, which seems to be exacerbated by every one of the new approaches of the ESAs within the consultation. Besides, we are convinced and want to give cause to serious concern that the best (i.e. most detailed) explanation will not be capable of solving the underlying problem of the current	

	methodology for the calculation and presentation of the performance scenarios itself. We doubt that by the current presentation of performance scenarios combined with *any* new or extended narrative the fair, clear and not misleading information which the investor would need can be provided.	
Q7	From a merely pragmatic point of view, some benefit may derive from the lengthening of the historical period. But we doubt that the disposability of the data can be handled without a significant increase of costs. We highly recommend to include the cost and data concerns in the ESAs' examination. We basically do not believe that a wider discussion on the overall methodology of the performance scenarios should be included in a consultation on "targeted amendments". We also note that the options raised by the ESAs have already been disregarded at an earlier stage in the Level-2 process which begs the question why they are brought back to the table in a consultation with such a narrow scope. While we understand that there are potentially other ways that disclosures can be calculated, any of these new methodologies and their outcomes must be rigorously tested and thoroughly assessed. In particular, they must be consumer tested to ensure that the information provided is of benefit to retail investors and does not have the serious potential to mislead investors, as is the case for the current performance scenarios. Again, such a discussion should take place as part of the wider Level-1 review of the PRIIPs Regulation and cannot be thoroughly undertaken in such a rushed and limited process as suggested by the ESAs and the European Commission.	
Q8	Our concerns to the integral changes to the performance scenarios are in line with our concerns on the changes to the methodology at this point in time. Again, these discussions must be undertaken under a proper Level-1 review. Any such changes should be thoroughly consumer tested. The ESAs' suggestion to limit the disclosure of performance scenarios to the stress and favourable scenarios is somewhat consistent with the requirements of Article 44 (fair, clear and not misleading information requirements) of the Commission Delegated Regulation 2017/565 to show both	

	negative and positive scenarios when disclosing future performance.	
Q9	Regarding the narratives for the Summary Risk Indicator (SRI) we note that the length limit was raised from 200 to 300 characters. As welcome as any increase in length is, it is still not nearly enough to properly explain additional risks to investors. There should be no character limit, thus allowing such disclaimers to be put in place by the PRIIP manufacturer, but – of course – having to keep within the overall PRIIP size limit. We would prefer the concrete designation of the additional risks analogue UCITS KIID as this method is familiar to the investors and most transparent. VOEIG does not see any additional benefit in the proposed changes to the MRM formula for e.g. fund-based saving plans. The outcome could culminate in two documents for the same product – or dealing with the latent size limit problem when creating two different presentations within the same document. Furthermore, the approach would have significant impact on data collections particularly with regard to the reporting obligations. When assessing section 4.2.1., we got the strong impression that an editorial mistake may have happened as the descriptions for category 2 and category 3 PRIIPs seem to be reversed (meaning the description for category 2 PRIIPs should be under the heading “category 3 PRIIPs” and vice-versa).	
Q10	We welcome the confirmation that the UCITS KIID framework is of such high importance in terms of properly disclosing information to investors that the ESAs are considering incorporating over 15 (of a total of 39) articles of the UCITS KIID Regulation (Regulation 583/2010) into the PRIIPs Level-2 Regulation. The sheer number of articles identified by the ESAs again showcases that the shift from the UCITS KIID to the PRIIP KID is no trivial matter. Given the ESAs’ very high-level and preliminary analysis, we expect that the proposed additions to the PRIIPS delegated acts will not be “targeted” but rather large in size. As the industry will not be able to see and comments on any of the detailed “UCITS additions” to the PRIIPs framework until they are sent to the co-legislators for approval early next year, we again must stress that this highlights the need to reinstate the original sequencing as laid out in Article 33	

| | of the Level-1 PRIIPs Regulation in order to produce a coherent and well-staged process that would result in the "phasing out" of the UCITS KIID.

On that very subject, we are surprised by the ESAs' comments on page 30: "*According to the UCITS Directive (Article 78), the UCITS KII currently needs to be provided not only to retail, but also to professional investors. Given that the PRIIPs Regulation applies to products made available to retail investors, the ESAs have worked under the assumption that should UCITS be required to provide a PRIIPs KID to retail investors the UCITS KII may still be provided to professional investors. However, this is also subject to any decision by the co-legislators on the exemption in Article 32 of the PRIIPs Regulation.*"

As mentioned above in our general remarks, there is no scope for professional investors within the UCITS KIID regime and never has been. We again underline that no additional benefit could be generated by producing a PRIIPs KID for retail investors and never let go of the UCITS KIID by keeping a second document only for professional investors (who, by the way, mostly don't need any additional documents to inform them about their products, because they are, as the designation implies, professionals and not retail investors). Many further questions would arise concerning the practical implementation of such a doubled system.

Furthermore, assuming that both a PRIIP KID and UCITS KIID are being produced would mean unwarranted resources that the fund industry will have to spend to produce two of such documents.

In cases where professional share classes are also open to retail investors, a situation could again arise where for the same fund, there are two different key information documents. Given the different methodology this will cause significant confusion for investors. How could the investor even distinct between the documents with visually matching, but materially different contents (e.g. SRI/SRRI charts), whether he is reading the document that is meant for him/her (the retail investor)? This is not in the investors' interest and will, operationally, be unfeasible to implement for firms.

Last but not least, if the UCITS KIID is not fully phased out, the ESAs' assessment to delete Article 12-14 of the Delegated Regulation regarding MOPs becomes null and void as certain products would still produce only UCITS data which would then have to be accepted by MOP producers. | |

	Overall, this again highlights the need for a proper Level-1 review as laid out in the PRIIPs Regulation.	
Q11	VOEIG would like to state that the switch over from the UCITS KIID to the PRIIP KID will carry substantial costs for the fund industry. As many IT budgets have already been decided for the next calendar year, such massive IT projects will consume unnecessary amounts of money and resources.	
Q12		
Q13	The situation is not made easier by the fact that there are many unresolved questions after having gone through the ESAs' consultation that make contingency planning for the "targeted" amendments even harder. The preliminary conclusion is that, the longer the process of the often demanded broad, proper and not only overarching, but also concluding re-conception of the PRIIPs KID regulation is postponed, the harder (respectively impossible) it becomes to even start the implementation process on a well-grounded basis.	