Position Paper

Insurance Europe response to a consultation by the European supervisory authorities on the technical discussion paper on PRIIPs

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Introduction

Insurance Europe welcomes the opportunity to respond to the European Supervisory Authorities' (ESAs) Technical Discussion Paper on the packaged retail and insurance-based investment products (PRIIPs). Insurance Europe supports the objective of the Regulation to enhance retail investor protection and improve retail investor confidence in PRIIPs. Moreover, Insurance Europe agrees that improving the transparency of the products offered to retail investors will contribute to this aim.

Insurance Europe appreciates ESA's work on development of the methodology that is suitable for all different PRIIPs and takes their specificities appropriately into account. However, the short consultation period, made it difficult to provide in-depth feedback on such important but challenging issues. Insurance Europe understands that the timeline is determined by the PRIIPs Regulation. However, it should be avoided that the time constrains and resulting short consultation periods will result in unsuitable or insufficiently thought through methodology for some PRIIPs.

It is of utmost importance that the features of insurance-based investment products are taken into account appropriately. These products provide for additional benefits and protection, in addition to offering an investment opportunity, such as guarantee of a given investment performance or a given level of benefits and protection against biometric risks (death benefits, occupational disability income, surviving dependents' provisions etc.). In this context, Insurance Europe would light to highlight its three key messages that are reflected throughout the paper.

First of all, it is not appropriate to include the biometric risk premium in the cost section of the KID. Premiums for protection against biometric risks are not costs, since the retail investor receives insurance benefits for these payments. Insurance Europe agrees that the biometric risk premium should be deemed a "price"' rather than a cost.

Secondly, reduction in yield (RIY) should be used as a cost indicator. In Insurance Europe's view, RIY is more suitable than the total cost ratio (TCR) since it can capture the costs of life insurance products appropriately and has the following main advantages when compared to the TCR:

- it takes into account the timing of costs

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- it is not based on the term "average investment" which is not a meaningful for insurance-based investment products

Thirdly, Insurance Europe believes that the what-if prescribed approach is valid and meaningful for PRIIPs. It is of utmost importance that the retail investors understand the performance scenarios.

Finally, Insurance Europe wishes to stress that the KID is provided at the pre-contractual stage and, therefore, is not a personalised document. It is, therefore, not appropriate to consider several KIDs dependent on the "age of the customer and other parameters". The retail investor will obtain personalised information later in the product distribution process. Should personalisation be considered at the pre-contractual phase, there will be an overlap notably with the insurance offer itself. Risk assessments for life insurance products take into account a large number of factors and criteria and age is only one factor that is taken into account. Age is not the only decisive biometric factor. Differentiation only according to it would not be appropriate and considering all the other factors would be unfeasible. Lastly, it seems also important to note that developing several KIDs for several ages for life-insurance products will have an effect on the compliance costs. This should be kept in mind especially because other PRIIPs manufacturers would not have to produce such a large number of KIDs. This would also lead to insurers providing retail investors with an overload of KIDs.

Detailed remarks

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.

It is important that the ESAs acknowledge the strong correlation between risk and reward.

It is of utmost importance that the retail investors understand the performance scenarios. Deterministic modelling is, therefore, more suitable for the performance scenarios.

It is important that an appropriate solution for the different objectives the KID is aiming to achieve is found (ie. comparability, legal certainty and helpful for retail investors). Modelling will be needed and the general principles of the models could be set at EU level.

Finally, since performance and costs of a PRIIP are strongly related, a consistent approach and presentation throughout the KID are needed.

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?

Firstly, as far as the risk indicator is concerned, Insurance Europe favours a quantitative indicator for market risk, complemented by qualitative credit risk information within the narrative explanation of the risks which are materially relevant for the PRIIP. The credit risk should not be integrated in the quantitative risk indicator. This would only add unnecessary complexity to the model.

In Insurance Europe's view, Option 1 is a good starting point for the risk indicator as it could be appropriate for many types of products and it would also be easy to implement by the industry, especially given the very short implementation timeline envisaged. Furthermore, it is easy to supervise and the criteria can be applied without difficulty.

But given that none of the proposals in the technical paper (including Option 1) appropriately cover every different type of product and in particular long-term insurance products with guarantees, an additional quantitative market risk measure suitable for long-term insurance products with guarantees could be appropriate in some markets, such as in Germany. However, the alternatively suggested based risk indicator which could be feasible for unit-linked insurance products, is not appropriate for long-term products with guarantees, since even the positive deviations from the mean will be regarded as risk. Therefore, for these products, alternatives should be developed. In other markets such an additional quantitative market risk measure will have no added value for long-term insurance products with guarantees.

As regards the performance scenarios, Insurance Europe considers that deterministic modelling is more suitable to facilitate retail investors' understanding. In addition, performance scenarios should be prescribed. Otherwise, there is a risk that the chosen scenarios are unreasonable and that retail investors cannot get comparable information. Moreover, only prescribed scenarios ensure legal certainty for PRIIPs manufacturers.

Only comparability within comparable classes should be envisaged. Otherwise, due to very differing time horizons (some days to several decades), a unifying approach would not lead to meaningful results for consumers.

Fine-tuning or detailing the assumptions in the regulatory technical standards (RTS) at EU level (such as setting the initial amount invested) might prove to be very difficult notably because of (1) the different spectrums of products available in different markets and (2) the differences in investment behaviour and capital at expense across the EU. This fine-tuning should be in line with consumer behaviour at national level.

- Setting similar assumptions for all products would most likely result in retail investors not receiving relevant information and certain products outperforming others based on the KID although they might not be the best fit for all retail investors. This is notably the case for insurance-based investment products providing additional benefits. As such, it is important that the level II measures do not result in information that might be confusing or even misleading to retail investors.

- In addition, as far as different investment behaviours are concerned, it is also of utmost importance to ensure that retail investors are not directed away from certain products that match their interests and investments on the basis of a KID only because it is not tailored to the features of the products appropriately. For example, the average investment by a retail consumer could significantly differ from country to country as a result of investor behaviour and/or average purchasing power.

In this context, high-level general principles for the performance scenarios should be set at EU level, while the fine-tuning or detailing of the assumptions to be used should be developed at a national level by the different PRIIPs manufacturers in cooperation with the local supervisory authorities to ensure a certain level of comparability between the different products and within certain product classes. This would also ensure that the assumptions and methodology used do not impact the product development and ultimately the product design.

See response to question 15 for the performance scenarios.

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?

The first option (ie. the amount invested without any adjustment) should be used as a benchmark notably because:

- The first option is the simplest and easiest to understand option for retail investors.
- The adjustment of the amount invested by the risk-free growth rate is not included in pre-contractual information disclosure for other products, such as the MiFID and UCITS for instance)
- Inflation is not a risk that is inherent only to PRIIPs but also affects other investment products that are excluded from the scope of the PRIIPs Regulation (eg. real estate, etc.).

Therefore, this information is not useful for retail investors nor does it increase comparability or transparency of products.

The definition of "loss" should be based on the option which is general, simple and most understandable and meaningful for retail investors. Therefore, the amount invested without any adjustment should be the level against which performance is measured.

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?

The asset growing 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 in time – ie. Option B) could be a good starting point to specify the growth rates. However, it is important that further simplifications are sought, in particular for products with a very long term. This is unproblematic since the performance scenarios for these products only indicate the uncertainty of return and do not predict the exact outcome.

Option A presented in the technical paper (ie. the asset grows at the risk free rate with the hypothesis that the risk premiums is equal to zero) is too unrealistic and therefore inadequate, given that assets' risk premia are almost never equal to zero. Option C (ie. the asset grows at the risk free rate adjusted for an asset specific risk premiums adjusted for the current market conditions) would result in an overly complex model.

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

For the timeframe in the risk indicator, Insurance Europe supports Option C presented in the technical paper. Only the risk indicator and performance scenarios for the holding period/ contractual terms are meaningful. Otherwise it would lead to confusing information and information overload for consumers. A warning or narrative text that explains the possible variation in risk over time is sufficient.

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

For insurance-based investment products market risk is the most relevant factor, whereas the credit and liquidity risks are more relevant for non-insurance PRIIPs.

As far as credit risk is concerned for insurance-based investment products, the Solvency II regime already incentivises the diversification of insurers' risks and ensures the financial capability of insurers to fulfil their contractual obligations, even under stressed conditions. In addition, in some countries, insurers' credit risk is further reduced thanks to insolvency guarantee schemes which should, therefore, be taken into account when assessing the credit risk. Depending on how credit risk is understood, the credit risk of the underlying financial instruments can be relevant for unit-linked products although it is key to stress that the credit risk of the underlying assets may end-up being already reflected in the PRIIP's market risk and should under no circumstances be accounted for twice.

Qualitative information regarding the credit risks could be added within the narrative explanation of the risks which are materially relevant for the PRIIP.
The credit risk should not be integrated in the quantitative risk indicator. This would only add unnecessary complexity to the model.

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?

Insurance Europe welcomes that the ESA distinguish liquidity risk from the liquidity profile of a product. The liquidity profile refers to characteristics of the product.

For insurance-based investment products market risk is the most relevant factor, whereas the liquidity risk can be relevant for certain non-insurance PRIIPs.

Regarding liquidity risk, retail investors usually purchase insurance-based investment products because they seek a long-term investment, which is a feature of the product rather than a risk.

The long-term nature should promote and encourage saving activity of consumers. This is why Insurance Europe welcomes the distinction between the liquidity risk and liquidity profile. In any case, early surrender should be discussed in another section of the KID ("How long should I hold it and can I take money out early?").However, for the products with significant liquidity risk, for example if the secondary market is not sufficiently active or there are no equivalent arrangements, e.g. early redemption rules, it should be captured in the risk/reward indicator.

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?

Insurance Europe welcomes that the ESA distinguish liquidity risk from the liquidity profile of a product. The liquidity profile refers to characteristics of the product. Insurance Europe supports purely qualitative measures for liquidity risks.

Liquidity risk seems to be much more relevant for non-insurance-based investment products. For insurance-based investment products, market risk is the most relevant factor. When discussing liquidity risk, it should be taken into account that a fixed term is in many cases a valuable feature for the customer and should therefore not be treated as a liquidity risk; otherwise this could wrongly lead to the product being described as an overall risky instrument in the summary risk/reward indicator.

The opposite is in fact true because the long-term nature should promote and encourage saving activity of consumers. In any case, early surrender should be discussed in another section of the KID ("How long should I hold it and can I take money out early?").

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

Insurance Europe regrets that none of the proposals in the technical paper appropriately cover every different type of product and in particular long-term products with guarantees.

For insurance-based investment products market risk is the most relevant factor, whereas the credit and liquidity risks are more relevant for non-insurance PRIIPs. Therefore, Insurance Europe favours a quantitative indicator for market risk, complemented by qualitative credit risk information within the narrative explanation of the risks which are materially relevant for the PRIIP. The credit risk should not be integrated in the quantitative risk indicator. This would only add unnecessary complexity to the model.

In Insurance Europe's view, Option 1 is a good starting point for the risk indicator as it could be appropriate for many types of products and it would also be easy to implement by the industry, especially given the very short implementation timeline envisaged. Furthermore, it is easy to supervise and the criteria can be applied without difficulty.

A weakness of this option is that risk bunching may occur when applying this indicator to insurance-based investment products. In some insurance markets like Germany, consumers are very interested in products with guarantees. Therefore, the overwhelming majority of products would fall into the same low risk category

(notwithstanding their otherwise different features). Conversely, in other insurance markets like the United Kingdom, retail investors typically accept more risk and a large number of different products would cluster around categories of higher risk. In both cases, the objective of discrimination would not be achieved.

Furthermore, in some markets, a marginal change in the products (such as 99.9% guarantee instead of a 100% guarantee) would change the risk-reward class of the product.

An additional quantitative market risk measure suitable for long-term insurance products with guarantees could be appropriate in some markets, such as in Germany. However, the alternatively suggested UCITS-based risk indicator which could be feasible for unit-linked insurance products, is not appropriate for long-term products with guarantees, since even the positive deviations from the mean will be regarded as risk. Therefore, for these products, alternatives should be developed. In other markets such an additional quantitative market risk measure will have no added value for long-term insurance products with guarantees.

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

Option 2 proposes an indicator separating assessment of market risk - quantitative measure based on volatility - and credit risk - qualitative measure, external credit ratings.

Insurance Europe sees a lot of drawbacks in this Option which stem from the fact that the type of indicator is appropriate for short-term products but inappropriate for long-term ones. The formula suggests that risk is proportionate to the level of guarantee and tenor, which is not the case for very long-term insurance-based PRIIPs. In addition, the formula is appropriate for linear risk structures, but wholly inappropriate for non-linear ones. Applying the indicator to these products would be artificial. Therefore, Insurance Europe strongly agrees with the second disadvantage listed by the ESAs in the technical paper, but also with all the other ones. In particular, Insurance Europe notes that this option may also not be legally viable given the separation of market and credit risk and would therefore conclude that this option should not be considered.

In most Member States, insurance products have terms of 10 years or more, whereas products with regular payments have usually terms of 30 years or more. The calculation of the aggregated volatility for a very short time, 5 or 20 days as described in the example followed by an approximation could be suitable for very short time periods (rather a couple of days than years). For long periods of 10 years or longer it is unreliable.

Insolvency guarantee schemes should be taken into account when assessing the credit risk. Moreover, Solvency II provisions ensure the financial soundness of insurers.

For these reasons, Insurance Europe does not support Option 2.

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

Option 3 proposes an indicator based on quantitative market and credit risk measures calculated using forward looking simulation models.

Insurance Europe agrees that this approach would ensure reliability and comparability once the parameters are determined as well as (unlike Option 1) discrimination including between different types of insurance-based PRIIPs. Furthermore, the model is neutral across all products in scope.

Should this option be considered further, it should be pointed out that:

- Credit risk is more relevant for non-insurance PRIIPs. Therefore, adding credit risk in the quantitative risk indicator would add unnecessary complexity to the model.
- The major premise of this type of indicator is that comparability of risks can only be achieved if an identical holding period for all products is set and applied. Insurance Europe considers that applying a

short holding period to a very long-term life insurance product would actually result in an unfair comparison with other types of PRIIPs.
- Finally, the resulting model could become complex and hard for manufacturers to implement.

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?

Option 3 proposes an indicator based on quantitative market and credit risk measures calculated using forward looking simulation models.

Insurance Europe agrees that this approach would ensure reliability and comparability once the parameters are determined as well as (unlike Option 1) discrimination including between different types of insurance-based PRIIPs.

Should this option be considered further, it should be pointed out that:

- Credit risk can only be relevant for certain types of insurance-based PRIIPs, namely unit-linked products. Therefore, adding credit risk in the quantitative risk indicator would add unnecessary complexity to the model.
- The major premise of this type of indicator is that comparability of risks can only be achieved if an identical holding period for all products is set and applied. Insurance Europe considers that applying a short holding period to a very long-term life insurance product would actually result in an unfair comparison with other types of PRIIPs.
- Finally, the resulting model could become complex and hard for manufacturers to implement.

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?

Option 4 proposes a "two-level" indicator.

The proposal for Option 4, as formulated in the Technical Discussion Paper, is too vague and many details are missing.

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?

Insurance Europe supports a risk indicator which has between 5 and 7 buckets scale. The specific risk scale should be examined during the consumer testing exercise.

Insurance Europe wishes to take this opportunity to note, however, that the summary risk indicator should be:

- Balanced to allow a clear categorisation of the different products.
- Take appropriately into account the long-term nature of insurance-based investment products.
- Neutral as far as design and colours are concerned to avoid any negative visual connotations linked to the risk categories.

A visualisation type similar to the UCITS key investor information document (KII) synthetic risk and reward indicator has all the above visual characteristics and would in addition allow for comparability with UCITS. It should be stressed that Insurance Europe supports the UCITS KII synthetic risk and reward indicator's presentation only, rather than the methodology behind it.

Since credit risk has little relevance for most insurance-based investment products, qualitative measures and generic criteria seem to be appropriate.

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

It is of utmost importance that the retail investors understand the performance scenarios. Deterministic modelling is, therefore, more suitable for the performance scenarios.

Practice and consumer testing[1] have shown that probabilistic modelling is often not understood by retail investors as opposed to deterministic modelling. Detailed analysis (also based on consumer testing) on this question has also been undertaken during for the key information disclosures for UCITS[2]. This clearly outweighs the benefits of probabilistic modelling.

Performance scenarios should be prescribed. Otherwise, it can neither be guaranteed that the chosen scenarios are reasonable nor that retail investors get comparable information. Moreover, only prescribed scenarios ensure legal certainty for PRIIPs manufacturers.

However, it is duly acknowledged that fine-tuning or detailing the assumptions at EU level (such as setting the initial amount invested) might prove to be very difficult notably because of (1) the different spectrums of products available in different markets and (2) the differences in investment behaviour and capital at expense across the EU. This fine-tuning should be in line with consumer behaviour at national level.

- Setting similar assumptions for all products would most likely result in retail investors not receiving relevant information and certain products outperforming others based on the KID, although they might not be the best fit for all retail investors. This is notably the case for insurance-based investment products providing additional benefits. As such, it is important that the level II measures do no result in information that might be confusing or even misleading to retail investors.

- In addition, as far as different investment behaviours are concerned, it is also of utmost importance to ensure that retail investors are not directed away from certain products that match their interests and investments on the basis of a KID only because it is not tailored to the features of the products appropriately. For example, the average investment by a retail consumer could significantly differ from country to country as a result of investor behaviour and/or average purchasing power.

In this context, high level general principles for the performance scenarios should be set up at EU level, while the fine tuning or detailing of the assumptions to be used should be developed at a national level by the different PRIIPs manufacturers in cooperation with the local supervisory authorities to ensure a certain level of comparability between the different products and within certain product classes. This would ensure that the assumptions and methodology used do not impact the product development and ultimately the product design.

[1] Cf for instance ABI "Research into presentation of risk and return to consumers"

[2] As CESR stated in its advice to the European Commission (see "CESR's technical advice to the European Commission on the format and content of Key Information Document disclosures for UCITS", 19 April 2010, Ref.: CESR/09-995, page 3) "The work carried out by CESR in that respect envisaged two possible options for performance scenarios:

- Option A: prospective scenarios showing the return of the fund under favourable, adverse and average market conditions;
- Option B: tables showing the probability of certain defined events: achieving a negative return or achieving a positive return worse, equal to or better than the risk-free rate.

A large majority of respondents to the consultations expressed a preference for Option A, prospective scenarios. Many of the respondents that supported Option A expressed strong disagreement with Option B on the basis that it would be misinterpreted as a guarantee and that the reliance on risk-neutral probabilities in the methodology was flawed. Option A was retained by CESR in its final advice."

In the same document (see page 22) CESR also "…considered carefully the merits and drawbacks of the two disclosure options for structured funds, as well as the comments made by respondents on each. Taking into account the support from a strong majority of respondents for Option A, prospective scenarios, CESR has confirmed this approach in its final advice. This choice is also based on the results of the Commission's consumer testing exercise, which showed that prospective scenarios lead to a good level of understanding by investors."

In addition, it is not useful and would be misleading for retail investors if the same number of scenarios was required for all products. The correlation of risk and performance is essential: the number of scenarios should depend on the risk class of a PRIIP. As a rule, fewer scenarios could be sufficient for less risky PRIIPs whereas the higher the risk class of a PRIIP, the wider the range between the scenarios should be. In this context and in line with Solvency II requirements[3] and other legislation[4] as well as to ensure that the investor is not over-burdened with irrelevant information, the Regulatory Technical Standards (RTS) should not require the presentation of more than three scenarios in the KID. A disclaimer should be added to explain that none of these three scenarios involve a stronger likelihood of occurrence.

Furthermore, it should be possible to present more scenarios if the manufacturer considers these scenarios to be relevant to the retail investors, for example in the case of products that include a specific pay-out mechanism that is activated under certain conditions.

Lastly, there are several elements that make insurance PRIIPs unique compared to other PRIIPs and that are very relevant in any comparison, such as the existence of insurance benefits (death benefit, disability cover, etc), as well as the long duration, the possibility to appoint a beneficiary, etc. The insurance sector believes that the additional benefits that are specific to insurance PRIIPs should not necessarily appear in the performance scenarios section of the KID. Instead, a separate section detailing the insurance cover, benefits and biometric risk premium should be in the KID. A reference to this separate section could be made in the performance scenario section, such as: "The additional benefits that are not related to the savings process are presented separately." Finally, Insurance Europe would like to point out that it is not appropriate to include biometric risk premium in the costs section of the KID. See answer to Question 45.

Furthermore, as regards death benefits, it is important to stress, that death benefits do not only consist of the payment in case of death. The beneficiary enjoys the protection during the entire term of a contract. This is a benefit in its own and cannot be measured in terms of a yield in the performance scenarios.

Finally, it is of utmost importance that the performance scenarios are consistent with the information on costs included in the cost section of the KID so that none of the features of the PRIIP is accounted for twice. If the performance scenarios are presented net of costs, it should be ensured that this is very clearly stated in the document and understood by retail investors.

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?

Insurance Europe believes that the what-if prescribed approach with defined scenarios is valid and meaningful for PRIIPs. High-level general principles for the performance scenarios should be set up at EU level, while fine-tuning or detailing of the assumptions to be used should be developed at a national level by the different PRIIPs manufacturers in cooperation with the local supervisory authorities to ensure a certain level of comparability between the different products and with certain product classes (see answer to question 15).

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

[3] Art. 185 of Solvency II states that where, in connection with an offer for or conclusion of a life insurance contract, the insurer provides figures relating to the amount of potential payments above and beyond the contractually agreed payments, the insurer shall provide the policy holder with a specimen calculation whereby the potential maturity payment is set out applying the basis for the premium calculation using three different rates of interest.

[4] Structured UCITS have to show at least three scenarios of the UCITS' potential performance. Appropriate scenarios have to be chosen to show the circumstances in which the formula may generate a low, a medium or a high return, including, where applicable, a negative return for the investor. The scenarios have to be based on reasonable and conservative assumptions about future market conditions and price movements.

It is of utmost importance that the retail investors understand the performance scenarios. Deterministic modelling is, therefore, more suitable for the performance scenarios.

Practice and consumer testing have shown that probabilistic modelling is often not understood by retail investors as opposed to deterministic modelling. Detailed analysis (also based on consumer testing) on this question has also been undertaken during for the key information disclosures for UCITS. This clearly outweighs the benefits of probabilistic modelling.

Performance scenarios should be prescribed. Otherwise, it can neither be guaranteed that the chosen scenarios are reasonable nor that retail investors get comparable information. Moreover, only prescribed scenarios ensure legal certainty for PRIIPs manufacturers.

However, it is duly acknowledged that fine-tuning or detailing the assumptions at EU level (such as setting the initial amount invested) might prove to be very difficult notably because of (1) the different spectrums of products available in different markets and (2) the differences in investment behaviour and capital at expense across the EU. This fine-tuning should be in line with consumer behaviour at national level.

- Setting similar assumptions for all products would most likely result in retail investors not receiving relevant information and certain products outperforming others based on the KID although they might not be the best fit for all retail investors. This is notably the case for insurance-based investment products providing additional benefits. As such, it is important that the level II measures do no result in information that might be confusing or even misleading to retail investors.

- In addition, as far as different investment behaviours are concerned, it is also of utmost importance to ensure that retail investors are not directed away from certain products that match their interests and investments on the basis of a KID only because it is not tailored to the features of the products appropriately. For example, the average investment by a retail consumer could significantly differ from country to country as a result of investor behaviour and/or average purchasing power.

In this context, high level general principles for the performance scenarios should be set up at EU level, while the fine tuning or detailing of the assumptions to be used should be developed at a national level by the different PRIIPs manufacturers in cooperation with the local supervisory authorities to ensure a certain level of comparability between the different products and within certain product classes. This would ensure that the assumptions and methodology used do not impact the product development and ultimately the product design.

In addition, it is not useful and would be misleading for retail investors if the same number of scenarios was required for all products. The correlation of risk and performance is essential: the number of scenarios should depend on the risk class of a PRIIP. As a rule, fewer scenarios could be sufficient for less risky PRIIPs whereas the higher the risk class of a PRIIP, the wider the range between the scenarios should be. In this context and in line with Solvency II requirements and other legislation as well as to ensure that the investor is not over-burdened with irrelevant information, the RTS should not require the presentation of more than three scenarios in the KID. A disclaimer should be added to explain that none of these three scenarios involve a stronger likelihood of occurrence. However, it should be possible to present more scenarios if the manufacturer considers these scenarios to be relevant to the retail investors and there is sufficient space on the document, for example in the case of products that include a specific pay-out mechanism that is activated under certain conditions.

Lastly, there are several elements that make insurance PRIIPs unique compared to other PRIIPs and that are very relevant in any comparison, such as the existence of insurance benefits (death benefit, disability cover, etc), as well as the long duration, the possibility to appoint a beneficiary, etc. The insurance sector believes that the additional benefits that are specific to insurance PRIIPs should not necessarily appear in the performance scenarios section of the KID. Instead, a separate section detailing the insurance cover, benefits and biometric risk premium should be in the KID. A reference to this separate section could be made in the performance scenario section, such as: "The additional benefits that are not related to the savings process are presented separately." See answer to Question 45.

18. Which percentiles do you think should be set?

It is of utmost importance that the retail investors understand the performance scenarios. Therefore, deterministic modelling with several different assumed returns is more suitable for the performance scenarios when these are used to illustrate the possible pay-outs.

Therefore, the what-if prescribed approach is more suitable.

19. Do you have any views on possible combinations?

It is of utmost importance that the retail investors understand the performance scenarios. Therefore, deterministic modelling with several different assumed returns is more suitable for the performance scenarios when these are used to illustrate the possible pay-outs.

The mix of deterministic and stochastic scenarios would confuse the consumers even further.

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

Coherence must be ensured throughout the KID.

Insurance Europe considers that, for, insurance-based investment products, market risk is the most relevant factor, whereas the credit and liquidity risks are more relevant for non-insurance PRIIPs. As far as credit risk is concerned for insurance-based investment products, the Solvency II regime already incentivises the diversification of insurers' risks and ensures the financial capability of insurers to fulfil their contractual obligations, even under stressed conditions. In addition, in some countries, insurers' credit risk is further reduced thanks to insolvency guarantee schemes which should, therefore, be taken into account when assessing the credit risk. In this context, Insurance Europe considers that the qualitative information regarding the credit risks could be added within the narrative explanation of the risks which are materially relevant for the PRIIP.

In order to ensure coherence throughout the KID, Insurance Europe considers that credit events should not be considered in the performance scenarios. Similarly as for the risk indicator, qualitative information regarding credit events could be added within the narrative explanation of the performance scenarios if materially relevant for the PRIIP.

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

Early redemption should be addressed in the section of KID on early surrender accordingly to Article 8(3)(g) of the PRIIP-Regulation which introduces a section in the KID called: *'How long should I hold it and can I take money out early?'*

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?

Insurance Europe believes that performance scenarios should only present potential return at the maturity of a life insurance product.

Early redemption should be addressed in the section of the KID on early surrender, accordingly to Article8.3.g of the PRIIP-Regulation which introduces a section in the KID called: *'How long should I hold it and can I take money out early?'*

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?

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

25. Should these fees be further specified?

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).

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).

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)?

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

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?)

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:

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

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?

34. Is this description comprehensive?

A copy paste of concepts that have been developed for investment products is neither meaningful nor feasible for life insurance products. The methods that exist for life insurance products should be used instead. See also our answer to question 41.

In addition, it should be highlighted that if the underlying fund a PRIIP invests in is not obliged to disclose certain costs, look through costs may not necessarily be known by the PRIIP manufacturer.

Regarding transaction costs, these are included in the costs for managing capital investments and should not be double counted: For life insurance products the total costs for managing capital investments are to be disclosed according to articles 34 (II) (9) and 42 of the Directive on the annual accounts and consolidated accounts of insurance undertakings (91/674/EEC). In addition, life insurers provide long-term products and, therefore, the investments of life insurers are mainly long term oriented, so the assets in their portfolios have often mid- to long-term maturities. Therefore, the frequency of reallocation is relatively rarely compared to other PRIIPs. So, the implicit transaction costs are marginal and negligible and without relevance for retail investors.

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

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?

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

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?

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?

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?

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?

As regards life insurance products, methods that already exist for these products should be used instead of adapting concepts developed for funds.

First, transaction costs that are included in the costs for managing capital investments should not be double counted: For life insurance products the total costs for managing capital investments are to be disclosed according to articles 34 (II) (9) and 42 of the Directive on the annual accounts and consolidated accounts of insurance undertakings (91/674/EEC).

Second, life insurers provide long-term products and, therefore, the investments of life insurers are mainly long term oriented, so the assets in their portfolios have often mid- to long-term maturities. Therefore, the frequency of reallocation is relatively rarely compared to other PRIIPs. So, the implicit transaction costs are marginal and negligible and without relevance for retail investors.

In any case, a proportionate, not overly burdensome, standardised, and simplified solution should be sought.

Finally, the insurance-related costs are included explicitly in the terms of the contract, are fixed and cannot be changed during the term of the contract. An appropriate and meaningful approach would be to use these costs as a basis for the calculation of costs. This approach is much more suitable for the insurance-based investment product than taking abstract costs borne by insurance undertaking as a starting point and splitting these to individual contracts.

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?

Yes, an explicit definition would be useful.

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?

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?

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).

The PRIIPs Regulation aims to ensure that retail investors are provided with accurate, fair and clear pre-contractual information to allow them to compare different investment products[5]. Should the biometric risk premium be considered as a cost, the information in the KID would be distorted and a proper comparison of PRIIPs would not be possible. In addition, it should be noted that Article 8(f) of the PRIIPs Regulation reads that the KID should include "the costs associated with an investment in the PRIIP" and does not refer to the biometric risk premium.

In this context, Insurance Europe believes that it is of utmost importance that the features of insurance-based investment products are properly taken into account within the PRIIPs KID. Insurance-based investment products have, per se, an insurance cover.

Unlike other PRIIPs, these products provide for:

- Additional benefits and protection, in addition to the investment opportunity, such as guarantee of a given investment performance or a given level of benefits (ensured through solvency requirements).
- Additional benefits and protection, which are not related to the investment opportunity, such as protection against biometric risks (death benefits, occupational disability income, surviving dependants' provisions etc.).

A correct definition of the "cost" term of an insurance-based PRIIP is essential for a useful KID. A sharp and clear distinction must be made between costs and premiums. Biometric risk premiums — which are payments that directly finance the benefits of a PRIIP — should never be considered as costs. Premiums are not costs, since the retail investor receives insurance benefits for these payments. Insurance Europe agrees that the biometric risk premium should be deemed a 'price' rather than a cost.

Even in theory, biometric risk premiums are not costs.

[5] Recital 15 of the PRIIPs Regulation states that the "*retail investors should be provided with the information necessary for them to make an informed investment decision and compare different PRIIPs ...*".

- Costs are the charges, that do not directly finance the benefit and which cover the expenses and the profit margin of the product designer or of other members of the value chain, such as distributors.
- The biometric risk premium provides retail investors with additional benefits, namely the insurance cover. Risk premiums are calculated according to the actuarial equivalence principle. This ensures that the retail investor receives the equivalent value in insurance benefits in exchange for the risk premium.

In this context, the insurance sector does not support one indicator that aggregates costs and biometric risk premiums. It is believed that such an indicator would be misleading and confusing for retail investors as well as create an unlevel regulatory playing field for PRIIPs:

- In order to compare investment-opportunities, retail investors should be provided with information to be in a position to compare what is comparable. The original purpose of the KID was to make substitute products comparable. Insurance-based investment products and pure investment products are, however, not substitutes. Insurance-based investments products have an investment element and an insurance element whereas pure investments products only have an investment element.
- If biometric risk premiums are included in costs, it would lead to the appearance of systematically higher costs of insurance-based investment products when compared to other products and would create an unlevel regulatory playing field. If biometric risk premiums are considered as costs the products will appear more expensive than they really are.
- According to research in the field consumers tend to give unbalanced prominence to the costs of a product, which distracts them from other crucial elements such as the insurance cover it comprises. Therefore, adding biometric risk premiums in the cost section would only give the consumer a distorted view of the product when compared to other products.
- In practice, the biometric risk premium cannot be communicated upfront in a pre-contractual phase as:
    - The biometric risk premium will depend on the personal characteristics of the person that needs to be insured.
    - The biometric risk premium will also depend on the individual choice of the consumer, i.e. the amount of insurance cover they seek.
    - For unit-linked products, the death cover depends on the development of the funds, which is unknown. Therefore, the actual amount of death cover is also unknown at the pre-contractual phase.

In practice, a single indicator would be non-transparent and lead to confusion. Different PRIIPs will not be comparable should both the costs and the biometric risk premiums for insurance-based investment products be included in one indicator. For instance:

- Example 1
    - A EUR 10,000 single-investment.
    - On death, the benefit is the value of the investment and an additional EUR 10,000 risk benefit.
    - The retail investor is 60 and the product term is 15-years.
    - The product has a simple 1% p.a. fund management charge and a charge for the risk benefit that is the approximate monthly cost of the cover.

  With this example over 15-years, the RIY is 2.4% p.a. which splits out as 1% p.a. for the investment costs and 1.4% p.a. for the biometric risk premiums. In this example, only 40% of the total RIY relates to the investment costs with 60% relating to the value of the benefits payable on death. It is, therefore, clear that this product would appear materially more expensive than an equivalent UCIT (undertaking for the collective investment of transferable securities) with a 1% fee.

- Example 2:
    - A with-profit life insurance product.
    - The retail investor is 35 and the product term is 30 years.
    - The regular premium is 1000 €/year and the death cover is 30.400 €.
    - The acquisition cost is 4% sum of all premiums and the regular costs is 8% of the premium/year.

- Its cost indicator is 0,91% RIY.
- If the premiums for death cover are treated as "costs", its "cost" indicator (together with the risk premium) would be 1,17% RIY (i.e. 30% higher).

This example demonstrates that an integrated cost indicator does not provide retail investors with the possibility to actually compare the products adequately.

There are many products that contain important risk cover. These products are also supported by governments with tax incentives in some countries. Retail investors are informed of both the costs and the benefits of the product, so they are fully aware that only part of the product is for investment. If the cost indicator includes biometric risk premiums, then this indicator will be relatively higher than other PRIIPs, and the retail investor will not be in a position to compare the investment part of the different products on the market.

The impact of a misleading cost indicator can be very detrimental to insurers offering insurance-based investment products. Should such a single aggregated indicator be introduced, an insurance-based investment product, which includes an investment element and insurance cover, would be presented as:

- The contribution is 100 €, with:
  - 75 € invested.
  - 25 € for costs.

What is presented to retail investors should rather be:

- The contribution is 100€, with:
  - 20 € is a premium / costs for insurance cover.
  - 80 € for the investment component, with:
    - 75 € invested.
    - 5 € for costs.

In the distorted presentation of the product, the costs for the product would suddenly be five times higher (20 € + 5 € = 25 € instead of 5 €). With such a presentation, a meaningful comparison would be possible neither with a pure investment PRIIP, nor with another insurance-based investment product.

Therefore, the inclusion of the biometric risk premium in the cost indicator of PRIIPs potentially disadvantages insurance products in comparison to other non-insurance PRIIPs and may also have a detrimental effect on the design of insurance products as companies may be forced to remove risk benefits in order to better compete.

In addition, Insurance Europe wishes to highlight that the representation of annualised costs together with a "reduction in yield (RIY)" approach is the most appropriate method for the cost representation, which is also very useful and understandable for retail investors. The RIY has two key advantages when compared to the total cost ratio (TCR):

- It takes into account the timing of costs.
- It is not based on the term "average investment", which is not a meaningful term and does not provide relevant information for life insurance products with regular contributions.

Insurance Europe suggests that information on the biometric risk premium be included in a separate section detailing the insurance cover, benefits and the biometric risk premium. In addition and to ensure complete transparency, a reference to this could be made in the cost section, such as: "The contributions for additional benefits that are not related to the savings process are presented separately."

There are several elements that make insurance PRIIPs unique compared to other PRIIPs and that are very relevant in any comparison, such as the existence of insurance benefits (death benefit, disability cover, etc), as well as the long duration, the possibility to appoint a beneficiary, etc. The insurance sector believes that the additional benefits that are specific to insurance PRIIPs should not appear in the performance scenarios section

of the KID. A reference to this separate section could be made in the performance scenario section, such as: "The additional benefits that are not related to the savings process are presented separately."

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

The breakdown of entry costs listed on page 76 of the ESAs Technical Paper includes a mix of (1) retail investors' costs for the product; and (2) insurers' expenses. It is necessary to separate the two in order to ensure that costs are not accounted for twice in the KID.

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper, referring to the main features of each of the costs: when and how often it is charged, the basis of this charge; and whether it is conditional or unconditional.

As far as the costs listed are concerned:

- A correct definition of the "cost" term of an insurance-based PRIIP is essential for a useful KID. A sharp and clear distinction must be made between costs and premiums. Premiums — which are payments that directly finance the benefits of a PRIIP — should never be considered as costs. Premiums for protection against biometric risks are not costs, since the retail investor receives insurance benefits for these payments (see response to question 45).

- Early redemption fees should not be treated as costs. These deductions are justified in accordance with actuarial principles and serve to protect the community of policyholders (e.g. against adverse selection). In Insurance Europe's view, it is important to inform retail investors about the possibility of early redemption or surrender value. However, this issue would be better addressed in the section of KID on surrender value.

- Embedded options, cost of holding required capital and guarantees of a given investment performance or a given level of benefits should be captured in the performance and risk section of the KID (more narrow spread between the performance scenarios, less risk). This is due to the fact that it is achieved by collective investment management, which is usually influenced by the corresponding legal provisions, e.g. in Solvency II, that enable insurance undertakings to design options and guarantees. The effect of capital guarantee on the risk/reward profile and performance scenarios should be treated consistently: the higher the guarantees, the lower the risk/reward class, and the more narrow the spread between the performance scenarios (e. g. a lower maximum value). This implies, however, that no fictitious, additional guarantee costs are assumed.

Finally, there is a strong correlation between costs and performance of the PRIIP. An integrated presentation of both is, therefore, necessary for the retail investors to understand the link between the two.

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?

The following specific features of insurance-based investment products are crucial and should be handled appropriately:

- Capital guarantee through solvency requirements behind the insurance-based investment products should be covered in the performance and risk section of the KID (more narrow spread between the scenarios, less risk).

- Insurance Europe welcomes ESA's suggestion not to treat early redemption fees as costs. These deductions are justified in accordance with actuarial principles and serve to protect the community of policyholders (e.g. against adverse selection). This issue would be better addressed in the section of

KID on surrender value. In Insurance Europe's view, it is important to inform retail investors about the possibility of early redemption or surrender value. Retails investors could be informed in a narrative way about these options in the KID.

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

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper referring to the main features of each of the costs: when and how often it is charged; the basis of this charge; and whether it is conditional or unconditional.

The insurance-related costs are included explicitly in the terms of the contract, are fixed and cannot be changed during the term of the contract. An appropriate and meaningful approach would be to use these costs as a basis for the calculation of costs. This approach is much more suitable for the insurance-based investment product than taking abstract costs borne by insurance undertaking as a starting point and splitting these to individual contracts.

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

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper referring to the main features of each of the costs: when and how often it is charged; the basis of this charge; and whether it is conditional or unconditional.

As far as the costs listed are concerned:

- Cost of holding required capital should be captured in the performance and risk section of the KID (more narrow spread between the performance scenarios, less risk). This is due to the fact that it is achieved by collective investment management, which is usually influenced by the corresponding legal provisions, e.g. in Solvency II, that enable insurance undertakings to design options and guarantees.

- As far as profit sharing is concerned, the insurance industry shares the view expressed in the ESAs technical paper that *"this issue is not easy to solve ex-ante".* Profit sharing could be problematic to show in some Member States because it is dealt at the level of the company rather than at the level of the individual contracts.

- Lastly, surcharges according to methods of regular payment chosen should not be considered as costs if they compensate the overestimated interest rates of a prospective calculation: Since not all premiums are due at the beginning of the year, the interest yield for the entire year should be reduced. This equally applies to all actuarially necessary surcharges.

In addition, it should be highlighted that if the underlying fund a PRIIP invests in is not obliged to disclose certain costs, look through costs may not necessarily be known by the PRIIP manufacturer.

In any case, double counting of costs should be avoided.

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

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper - ie. The main features of each of the costs; when and how often it is charged, the basis of this charge and whether it is conditional or unconditional.

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

A correct definition of the "cost" term of an insurance-based PRIIP is essential for a useful KID. A sharp and clear distinction must be made between costs and premiums. Premiums — which are payments that directly finance the benefits of a PRIIP — should never be considered as costs. Premiums for protection against biometric risks are not costs, since the retail investor receives insurance benefits for these payments (see response to question 45).

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper - ie. The main features of each of the costs; when and how often it is charged, the basis of this charge and whether it is conditional or unconditional.

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

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper - ie. The main features of each of the costs; when and how often it is charged, the basis of this charge and whether it is conditional or unconditional.

Insurance Europe welcomes ESA's suggestion not to treat early redemption fees as costs. These deductions are justified in accordance with actuarial principles and serve to protect the community of policyholders (e.g. against adverse selection). This issue would be better addressed in the section of KID on surrender value. In Insurance Europe's view, it is important to inform retail investors about the possibility of early redemption or surrender value. Retails investors could be informed in a narrative way about these options in the KID.

It is key to ensure that double counting of costs is avoided.

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?

Insurance Europe welcomes ESA's suggestion not to treat early redemption fees as costs. These deductions are justified in accordance with actuarial principles and serve to protect the community of policyholders (e.g. against adverse selection). This issue would be better addressed in the section of KID on surrender value. In Insurance Europe's view, it is important to inform retail investors about the possibility of early redemption or surrender value. Retails investors could be informed in a narrative way about these options in the KID.

As far as the fund related costs are concerned, Insurance Europe wishes to point out the need to ensure a level playing field between unit-linked and hybrid life-insurance products.

Insurance Europe believes that it is not necessary to further specify the methodology for the calculation of the fund related costs.

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

Insurance Europe wishes to point out the need to ensure a level playing field with between unit-linked and hybrid life-insurance products. In addition, it seems relevant to highlight that the look-through costs will need to be estimated.

If the underlying of a PRIIP is not a PRIIP itself, then the manufacturers might not be able to provide all the information for the underlying which is required by the PRIIPs Regulation since there is no full "look-through". This applies for example to UCITS funds, which are not obliged to disclose transaction costs. In this case, it should be ensured that the manufacturers are only obliged to disclose the information they are legally entitled to receive from the investment management companies.

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

Insurance Europe believes that the relevant points that must be taken into account, when identifying the costs, are correctly identified by the ESAs in page 52 of the technical paper - ie. The main features of each of the costs; when and how often it is charged, the basis of this charge and whether it is conditional or unconditional.

Insurance Europe believes that it is not necessary to further specify the methodology for the calculation of these costs.

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?

First of all, it is of utmost importance that no costs are accounted for twice in the PRIIPs' KIDs.

In addition, the biometric risk premium should not be considered as a cost. A correct definition of the "cost" term of an insurance-based PRIIP is essential for a useful KID. A sharp and clear distinction must be made between costs and premiums.

Insurance Europe appreciates that ESA recognise the importance of costs surpluses being deduced from the costs and taken into account in the costs section of the KID.

As already stated in the answer to Q48, the insurance-related costs are included explicitly in the terms of the contract, are fixed and cannot be changed during the term of the contract. An appropriate and meaningful approach would be to use these costs as a basis for the calculation of costs. This approach is much more suitable for the insurance-based investment product than taking abstract costs borne by insurance undertaking as a starting point and splitting these to individual contracts.

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?

Costs for managing capital investments are not specific to with-profit products; these costs apply as well to other PRIIPs.

As already stated in the answer to Q48, the insurance-related costs are included explicitly in the terms of the contract, are fixed and cannot be changed during the term of the contract. An appropriate and meaningful approach would be to use these costs as a basis for the calculation of costs. This approach is much more suitable for the insurance-based investment product than taking abstract costs borne by insurance undertaking as a starting point and splitting these to individual contracts.

In Insurance Europe's view, since the costs for managing capital investments are not comparable and less relevant for insurance-based investment products, a proportionate, not overly burdensome solution needs to be found instead of copy and pasting the funds concept. For example, the differentiation of costs is not necessary in the profit and loss account: For life insurance products only the total investment costs are to be disclosed according to articles 34 (II) (9) and 42 of the Directive on the annual accounts and consolidated accounts of insurance undertakings (91/674/EEC).

As regards transaction costs, those that are already included in the administration costs as described above should not be double counted. Furthermore, life insurers provide long-term products and, therefore, the investments of life insurers are mainly long term oriented, so the assets in their portfolios have often mid- to

long-term maturities. Therefore, the frequency of reallocation is relatively rarely compared to other PRIIPs. So, the implicit transaction costs are marginal and negligible and without relevance for retail investors. In any case, a proportionate, standardised, and simplified solution should be sought.

Insurance Europe welcomes that the ESA acknowledge surcharges according to methods of regular payment chosen not being regarded as costs, but interest income contribution due to late payment. This equally applies to all actuarially necessary surcharges. Costs for regular payments for periods of less than a year are calculated separately.

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

The list of costs is comprehensive. However, once again, Insurance Europe would like to point out:

- Biometric risk premiums are not costs, since the retail investor receives insurance benefits for these payments.
- Embedded options, costs of holding capital and capital guarantee protecting against market risk of the insurance-based investment products should be covered in the performance and risk section of the KID (more narrow spread between the performance scenarios). In general, performance scenarios should be consistent with the information on costs included in the cost section of the KID: the higher the guarantees, the lower the risk class, and the more narrow the spread between the performance scenarios (e. g. a lower maximum value). This implies, however, that no fictitious, additional guarantee costs are assumed.
- Early redemption fees should not be treated as costs. These deductions are justified in accordance with actuarial principles and serve to protect the community of policyholders (e.g. against anti-selection). Then again, this issue should be better addressed in the section of KID on surrender value. In our view, it is important to inform the retail investors about the development of the surrender value of their PRIIP. Due to the limitation of the length of the document at least the ratio "surrender value / sum of contributions" should be presented for, say, 1, 5 10, 20 and 30 years.
- The actuarially justified surcharges according to the methods of regular payment chosen in the premium calculation should be not considered as costs.

If the underlying fund a PRIIP invests in is not obliged to disclose certain costs, look through costs may not necessarily be known by the PRIIP manufacturer.

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

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?

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?

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

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?

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?

65. Would you include other cost components?

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

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?

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)?

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

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

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?

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

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?

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

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?

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

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?

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

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?

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).

Insurance Europe is of the opinion that the Regulation does not ask for record keeping period of each calculation and, therefore, sees no need for the ESAs to establish one.

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

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?)

The total cost should be presented in monetary terms per year (annual average) and percentage terms. Indeed the specificities of the insurance-based investment products (ie. very long duration) should be duly taken into account. An option presenting the total costs for the whole investment period would not allow for an effective comparison between, for example, a product with a few months investment period and one characterised by a 35 years investment period.

Depending on the nature of the product (investment or saving product), differences in the types of premiums (single, regular or other) should be taken into account.

It would also be difficult to set assumptions that would work for all products all over the European Union.

- First of all, artificially setting and obliging manufacturers to use assumptions which do not fit their products would not help retail investors get a good overview of costs. Setting similar assumptions for all products would most likely result in retail investors not receiving relevant information and certain products outperforming others based on the KID although they might not be the best fit for all retail investors.

- In addition, as far as different investment behaviours are concerned, it is also of utmost importance to ensure that retail investors are not directed away from certain products that match their interests and investments on the basis of a KID only because it is not tailored to the features of the products appropriately. For example, the average investment by a retail consumer could significantly differ from country to country as a result of investor behaviour and/or average purchasing power.

In this context, high-level general principles should be set at EU level, while the fine-tuning or detailing of the assumptions to be used should be developed at a national level by the different PRIIPs manufacturers in cooperation with the local supervisory authorities to ensure a certain level of comparability between the different products and within certain product classes. This would also ensure that the assumptions and methodology used do not impact the product development and ultimately the product design.

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?

As noted in the response to Question 45, a correct definition of the "cost" term of an insurance-based PRIIP is essential for a useful KID. A sharp and clear distinction must be made between costs and premiums. Premiums — which are payments that directly finance the benefits of a PRIIP — should never be considered as costs. Premiums for protection against biometric risks are not costs, since the retail investor receives insurance benefits for these payments. In this context, the costs will not differ on the age of the customer and other parameters.

It should also be noted that the KID is provided at the pre-contractual stage and, therefore, is not a personalised document. It is, therefore, not appropriate to consider several KIDs dependent on the "age of the customer and other parameters". The retail investor will obtain personalised information later in the product distribution process. Should personalisation be considered at the pre-contractual phase, there will be an overlap notably with the insurance offer itself.

The insurance sector wishes to point out that risk assessments for life insurance products take into account a large number of factors and criteria. Age is only one factor that is taken into account. Differentiation only according to it would not be appropriate and considering all the other factors would be unfeasible. In this context, the insurance sector does not consider that several KIDs for several ages would be suitable.

Lastly, it seems also important to note that developing several KIDs for several ages for life-insurance products will have an effect on the compliance costs. This should be kept in mind especially because other PRIIPs manufacturers would not have to produce such a large number of KIDs. This would also lead to insurers providing retail investors with an overload of KIDs.

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

Insurance Europe wishes to highlight that the representation of annualised costs together with a RIY approach is the most appropriate method for the cost representation, which is also very useful and understandable for retail investors. The RIY has two key advantages when compared to the total cost ratio (TCR):

- It takes into account the timing of costs.
- It is not based on the term "average investment", which is not a meaningful term and does not provide relevant information for life insurance products with regular contributions.

As a good illustration, when comparing the two products presented in the tables pages 123 and 124 of the technical paper, it is clear that the RIY is the most suitable measure to allow retail investors to compare products. The TCR method does not allow the retail investor to differentiate between the two products.

Since the insurance-based investment products have terms that sometimes last over decades, only annualised costs are comparable for different PRIIPs in a consistent, robust and stable way. This becomes particularly obvious if products that have a term of three months are compared with products that have duration of 30 years. Therefore, it is important to apply a suitable, transparent, comprehensive and comparable cost indicator. In Insurance Europe's view, the RIY approach is the most appropriate method for the cost representation since it fulfils the above mentioned requirements.

The biggest disadvantage of TCR – inability to take into account the effects of interest – could be negligible for contracts with a short term. If in these cases the TCR produces equivalent results, it could be also applied instead of RIY. However, it is clear that only RIY provides meaningful cost indicators for products with long maturities.

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?

In Insurance Europe's view, the TCR is not a feasible indicator to capture the costs of life insurance products appropriately and, therefore, should not be used. The TCR has the following two major caveats:

- It does not take into account the timing of costs: this is particularly important if a product has significant acquisition costs.
- It is based on the term "average investment" which is not a meaningful term and does not provide relevant information for life insurance products with regular contributions.

The examples on pages 123 and 124 illustrate the above mentioned problem. While the TCR produces almost the same number irrespective of whether the costs are due in the beginning of the contract or not, RIY provides a more reliable number.

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?

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The biggest disadvantage of TCR – inability to take into account the effects of interest – could be negligible for contracts with a short term. If in these cases the TCR produces equivalent results, it could be also applied instead of RIY. However, it is clear that only RIY provides meaningful cost indicators for products with long maturities.

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?

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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?

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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?

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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?

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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?

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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.

Insurance Europe entirely agrees with the difficulties and drawbacks elaborated by the ESAs. In Insurance Europe's view, quantification is neither meaningful nor necessary.

First of all, embedded options and capital guarantee protecting against market risk should be covered in the performance and risk section of the KID (more narrow spread between the performance scenarios). This is due to the fact that it is achieved by collective investment management, which is usually influenced by the corresponding legal provisions, e.g. in Solvency II that enables insurance undertakings to design options and guarantees. The effect of capital guarantee on the risk/reward profile and performance scenarios should be treated consistently: the higher the guarantees, the lower the risk/reward class, and the more narrow the spread between the performance scenarios (e. g. a lower maximum value). This implies, however, that no fictitious, additional guarantee costs are assumed.

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

In Insurance Europe's view the RIY approach can be applied to funds.

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?

In Insurance Europe's view the RIY approach can be applied to structured products. The difficulties that are stated to be specific to RIY, exist in the same way for TCR.

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?

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Finally, since risks and reward as well as performance and costs of a PRIIP are strongly correlated, a consistent approach and presentation of these features throughout the KID are needed.

In Insurance Europe's view, the calculation basis for returns should be investment gross amount before costs. It is important to correctly specify this amount: e.g. if the products guarantees a certain minimum yield, then a 0% gross performance is not appropriate.

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

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

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

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