JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

16 October 2019

JC 2019 63

Joint Consultation Paper concerning amendments to the PRIIPs KID

Draft amendments to Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 on key information documents (KID) for packaged retail and insurance-based investment products (PRIIPs).

Contents

1. Responding to this Consultation

The European Supervisory Authorities (ESAs) welcome comments on this consultation paper setting out proposed amendments to Commission Delegated Regulation (EU) 2017/653 of 8 March 2017[1] (hereinafter "PRIIPs Delegated Regulation").

The consultation package includes:

- The consultation paper
- Template for comments

The ESAs invite comments on any aspect of this paper. Comments are most helpful if they:

- contain a clear rationale; and
- describe any alternatives the ESAs should consider.

When describing alternative approaches the ESAs encourage stakeholders to consider how the approach would achieve the aims of Regulation (EU) No 1286/2014[2] (hereinafter "PRIIPs Regulation").

Submission of responses

The consultation paper is available on the websites of the three ESAs and the Joint Committee. Comments on this consultation paper can be sent using the response form, via the ESMA website under the heading 'Your input - Consultations' by **13 January 2020**.

Contributions not provided in the template for comments, or after the deadline will not be processed.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESAs rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESAs Board of Appeal and the European Ombudsman.

Data protection

[1] COMMISSION DELEGATED REGULATION (EU) 2017/653 of 8 March 2017 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products (PRIIPs) by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents

[2] Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs), OJ L 352, 9.12.2014, p. 1.

The protection of individuals with regard to the processing of personal data by the ESAs is based on Regulation (EU) 2018/1725[3]. Further information on data protection can be found under the Legal notice section of the EBA website and under the Legal notice section of the EIOPA website and under the Legal notice section of the ESMA website.

[3] Regulation (EU) 2018/1725 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and Decision No 1247/2002/EC, OJ L 295, 21.11.2018, p. 39.

2. Context and approach to the review

2.1 Introduction

This Consultation Paper proposes amendments to the PRIIPs Delegated Regulation. The main aims of the review are to:

- Allow the appropriate application of the PRIIPs KID by UCITS and relevant non-UCITS funds[4], subject to the potential end of the temporary exemption of such funds from the requirements of the PRIIPs Regulation (see next section below);

- Address the main regulatory issues that have been identified since the implementation of the PRIIPs KID to those products that are currently in scope.

These proposals follow a previous consultation paper of the ESAs in November 2018 (CP 2018 60) (hereinafter “November 2018 CP”), which had similar aims, but which proposed more targeted amendments to the PRIIPs Delegated Regulation. Based on the feedback received to that consultation, as well as based on the decision by the co-legislators to extend the exemption for UCITS, the ESAs decided in February 2019 to defer their review and launch a public consultation on more substantive changes later in 2019.

2.2 UCITS exemption and ESAs’ targeted review proposals

The PRIIPs Regulation provides a temporary exemption for management and investment companies and persons advising on, or selling, UCITS from the obligation to produce and provide a PRIIPs KID (Article 32). For such funds, a Key Investor Information (KII) document is currently provided to investors in accordance with Directive 2009/65/EC[5] (hereinafter “UCITS Directive”). This exemption was originally due to expire on 31 December 2019.

In the autumn of 2018, the ESAs initiated a targeted review of the PRIIPs Delegated Regulation. This was in view of the potential end of the exemption for UCITS at the end of 2019, and to address some issues that had arisen since the application of the PRIIPs Regulation at the beginning of 2018. A consultation paper was published on 8 November 2018. In order for these amendments to be implemented by the end of 2019 a shortened public consultation was necessary and the ESAs announced their aim to conclude their work during January 2019.

During the autumn of 2018, the co-legislators also initiated discussions on potential changes to the PRIIPs Regulation to address the UCITS exemption, as well as the timing of a review of the PRIIPs

[4] The exemption also applies to non-UCITS funds in Member States which extend the application of UCITS rules on the format and content of the UCITS key investor information to non-UCITS made available to retail investors (Article 32(2) of the PRIIPs Regulation).

[5] DIRECTIVE 2009/65/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

Regulation. The ESAs' proposals in their consultation paper were therefore made in the context of uncertainty as to the outcome of these ongoing political discussions.

In response to the public consultation, overall stakeholders did not support the ESAs' proposals to make targeted amendments at that time. By January 2019, there had also been an informal agreement between the co-legislators to extend the exemption for UCITS until 31 December 2021 (amendment to Article 32 of the PRIIPs Regulation). Taking these developments into account, the ESAs decided that it would not be appropriate to propose amendments to the PRIIPs Delegated Regulation at that time.

Instead, when publishing their Final Report to the consultation on 8 February 2019 (JC 2019 6.2) (hereinafter "February 2019 Final Report"), the ESAs announced their intention to undertake a more comprehensive review of the PRIIPs Delegated Regulation taking into account the additional two years before UCITS might be required to produce a PRIIPs KID.

Shortly afterwards, the co-legislators formally agreed to extend the date in Article 32 of the PRIIPs Regulation until the end of 2021. As things stand, in the absence of legislative changes, from 1 January 2022, UCITS will be required to prepare a PRIIPs KID and UCITS KII. In view of this, the European Commission are expected to table legislative proposals in due course to address the requirements that would apply to UCITS from 1 January 2022 onwards.

2.3 Scope of the current review

The February 2019 Final Report set out how the ESAs planned to conduct the work and the main areas of the PRIIPs KID that they intended to analyse. This included, as well as specific issues related to the potential end of the UCITS exemption, the following topics: performance scenarios, costs, and PRIIPs offering a range of investment options (MOPs)[6].

It was also stated that:

> *the ESAs intend to focus their work on the need for amendments to the PRIIPs Delegated Regulation...However, where the information collected and analysis conducted on the application of the KID during the course of this work would indicate that changes to the PRIIPs Level 1 Regulation may be needed in order to achieve the optimal outcomes in relation to the requirements in the PRIIPs Delegated Regulation, the ESAs will consider whether it is relevant to additionally recommend such changes to the co-legislators.*

A review of the PRIIPs Regulation was originally envisaged to take place by 31 December 2018. However, earlier this year, the co-legislators decided to extend this date until 31 December 2019. In view of this revised deadline, the ESAs understand that the European Commission are preparing to initiate a review of the PRIIPs Regulation. However, it is not expected that all of the different elements of the review required by Article 33 of the PRIIPs Regulation will be completed by the end of this year.

[6] See page 13 and 14 of the February 2019 Final Report. The ESAs also highlighted the more general theme that they would look at the need for further differentiation between different types of PRIIPs, and other specific changes.

In addition, some parts of that review, in particular regarding the exemption for UCITS, may need to be addressed separately given their specific timing constraints.

The ESAs have not included any specific recommendations to change the PRIIPs Regulation within this consultation paper. The ESAs are however conscious that some of the concerns expressed by stakeholders relating to performance scenarios, costs and MOPs might not be entirely resolvable through a change in the PRIIPs Delegated Regulation.

It can also be noted that for some of the options to amend the requirements for performance scenarios in the PRIIPs Delegated Regulation discussed in this consultation paper, concerns have been raised by the European Commission as to whether these options fully comply with the current PRIIPs Regulation.[7] However, the decision on these options remains open, subject to feedback from this public consultation and a consumer testing exercise (for the latter see Section 4).

For the other topics addressing amendments to the PRIIPs Delegated Regulation within this consultation paper, for example regarding costs, the proposals are considered to be in line with the current PRIIPs Regulation. At the same time, the ESAs might still consider making recommendations to change the PRIIPs Regulation in these areas. This would be based on the feedback received from stakeholders as to whether the proposed amendments are likely to address the issues identified and facilitate the understanding of retail investors.

Feedback is also requested from stakeholders on a limited number of additional issues that may require changes to the PRIIPs Regulation, for example concerning the use of the UCITS KII for professional investors (see Section 9). As part of this approach, the ESAs would be interested in stakeholders' views on several overarching issues concerning the use of KID in the context of digital innovation.

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

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

Overall, the ESAs will consider whether targeted recommendations to change the PRIIPs Regulation are needed when deciding on their final proposals.

2.4 Intended timeline and next steps

In the February 2019 Final Report it was stated that the ESAs intended to finalise their work to review the PRIIPs Delegated Regulation by the end of 2019. This took into account, on the one hand, the revised deadline in Article 32 of the PRIIPs Regulation, while, on the other hand, the expected benefit of changes to the PRIIPs Delegated Regulation being applied to existing PRIIPs as soon as practicable.

[7] See Section 4.2 below.

Following subsequent discussions with the European Commission regarding the possibility to test proposals on consumers and the timing of such an exercise, as well as regarding the timing of potential legislative proposals to address the requirements that would apply to UCITS from 1 January 2022 onwards, the ESAs now intend to conclude their review around the end of the first quarter 2020 and submit their final proposals to the European Commission shortly afterwards. These would then be subject to endorsement by the European Commission, following which the European Parliament and Council would be given the opportunity to express any objections to the amending regulatory technical standards (RTS) as adopted by the European Commission.

Subject to these endorsement procedures and an adequate implementation period for market participants, the amendments proposed to the PRIIPs Delegated Regulation in this consultation paper could be applied to existing PRIIPs during 2021 before the expected end of the UCITS exemption.

At the same time, there could be arguments to defer the application of some of the proposed amendments to be aligned with the expected end of the UCITS exemption. This could include, for example, the potential inclusion in the PRIIPs KID of past performance.

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

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

3. Overview of the Consultation Paper and next steps

3.1 Overview of Consultation Paper

This consultation paper provides stakeholders with an opportunity to comment on proposed amendments to the PRIIPs Delegated Regulation.

These amendments relate to the empowerment in Article 8(5) of the PRIIPs Regulation concerning the presentation and content of the KID, including methodologies for the calculation and presentation of risks, rewards and costs within the document.

Section 4 of the consultation paper discusses changes to the presentation of performance information which are part of a parallel consumer testing exercise being conducted by the European Commission with the involvement of the ESAs.

Sections 5 to 10 discuss the nature of the proposed amendments to each of the topic areas in turn as follows:

- Section 5 presents proposals to change the methodology for performance scenarios, including some evidence to support the approach;
- Section 6 discusses a possible alternative to present illustrative performance scenarios;
- Section 7 sets out how past performance information could be included in the KID;
- Section 8 presents different options to change the methodologies to calculate costs and how these are presented in summary tables;
- Section 9 considers possible changes in view of the exemption in Article 32 of the PRIIPs Regulation being due to expire and the possible use of the PRIIPs KID by UCITS from 1 January 2022;
- Section 10 presents proposals to amend the rules related to PRIIPs offering a range of options for investment.

Section 11 includes an example KID relating to the proposals in Section 10.

Section 12 sets out the legislative amendments in the form of an amending RTS that would be needed for each of the proposals or options in turn.

Preliminary analysis of the expected costs and benefits of the proposed amendments is also included in the consultation paper (in **Section 13**), in order to gather feedback on possible costs and benefits of the proposals and the relative scale of these costs and benefits for different stakeholders.

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

4. Consumer testing

4.1 Introduction and explanation of the different options to present performance information being considered

The ESAs stated in the February 2019 Final Report that they would work with the European Commission regarding the possibility to test both the existing KID approaches and new proposals on consumers. Within the timeframe of the current review of the PRIIPs Delegated Regulation, it will not be possible to test all aspects of the KID.

However, the European Commission, with the assistance of the ESAs, have initiated a targeted consumer testing exercise to assess the effectiveness of different presentations of performance information. This testing is being led by the European Commission in close co-operation with the ESAs and the content of the testing is based on options proposed by the ESAs. This includes options regarding performance scenarios and past performance, which are explored further in this paper.

The timeframe for conducting consumer testing meant that the presentation options were drafted at an early stage in the review process. The results of this testing are expected to be provided in the first quarter of 2020. As a result, this consultation is not able to provide a final proposal for how performance information will be presented in the KID. At this stage, the draft proposals set out in Section 12.1 of this consultation paper include a revised template for the performance scenarios (Annex V of the PRIIPs Delegated Regulation) based on the proposals developed for the consumer testing.

When finalizing the performance scenario templates, some changes are expected to ensure that they are fully aligned with the final performance scenario methodology, as well as to reflect a decision on the following main aspects that are yet to be determined:

- whether intermediate scenarios (future scenarios for periods shorter than the recommended holding period) should be included;
- whether to indicate in the performance scenario table the estimated probability of each scenario;
- whether a fourth (stress) scenario should be included or alternatively a row showing the minimum investment return;
- whether past performance should be included in addition to forward looking performance scenarios; and,
- whether an illustrative approach (not based on probabilities) to future performance scenarios should be used.

The decision on these aspects will be made when their effectiveness in enhancing consumer understanding is assessed using the results of the consumer testing.

The ESAs will also fully consider the opinions from stakeholders on the options proposed and their applicability to different types of PRIIPs, as well as regarding any alternative proposals that should be considered.

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

4.2 Development of options for the consumer testing

When preparing the options for testing during the first half of this year, it was necessary to identify the different types of approaches for performance scenarios that were considered as the most viable alternatives (to the current KID). As part of this work, as stated in the February 2019 Final Report, the ESAs evaluated the approach of only showing qualitative information regarding potential future performance, for example regarding the factors that affect future performance. Some stakeholders have argued that the disclosure of any figures creates a risk that investors will attach an inappropriate degree of certainty to these figures. While such an approach would clearly limit this risk, the ESAs judged that this would likely result in generic information being provided to investors that would not be informative or facilitate their comparison between different types of products. Consequently, the ESAs did not consider this to be a viable option to propose for inclusion in the consumer testing.

On 23 May 2019, the ESAs submitted their proposed options[8] to be tested to the European Commission[9]. The ESAs proposed to test options involving:

- The use of the current KID in order to gather evidence on the effectiveness of the current presentation;

- A revised presentation and structure of the performance scenario table (but still based on a probabilistic methodology to estimate possible future outcomes – see Section 5 for a discussion of methodologies)

- The use of illustrative performance scenarios for certain types of PRIIPs to show the behaviour of the product in different hypothetical market circumstances. For insurance-based investment products, it was proposed to test the use of such scenarios in addition to probabilistic scenarios. For structured products, it was proposed to test the use of only illustrative scenarios (instead of probabilistic scenarios), as well as showing both probabilistic and illustrative scenarios.

[8] JC 2019 46

[9] For the purposes of proposing options to be tested, the ESAs used example products for an investment fund, an insurance-based investment product and a structured product. As part of the further preparation of the consumer testing, the ESAs have worked with the European Commission to develop additional example products.

- The inclusion of information on past performance (in addition to probabilistic scenarios) for certain types of PRIIPs. For funds, the presentation of past performance is based on the bar chart established in the Commission Regulation (EU) No 583/2010[10] (hereinafter "UCITS Regulation 583/2010"). For IBIPs, it was proposed to also test some alternative presentations, including showing average performance over different time periods rather than annual figures.

On 19 July 2019, the European Commission informed the ESAs that three of the proposed options will not be included in the consumer testing on the basis of their compliance with the PRIIPs Regulation and their practical feasibility. These three options are:

- For structured products, the use only of illustrative performance scenarios (Option 4 proposed by the ESAs);

- For IBIPs:

    - The inclusion of illustrative scenarios showing the performance drivers and returns at different time periods as well as probabilistic scenarios (Option 5 proposed by the ESAs);

    - The inclusion of past performance information showing average performance over different time periods (Option 6 proposed by the ESAs).

The ESAs did not support the restriction of the scope of the consumer testing exercise. Therefore, in a response[11] to the Commission on 30 July 2019, they stated that they would still consider including these options when consulting stakeholders on proposed amendments.

The subsequent Sections of this consultation paper discuss the rationale for and types of amendments that would be needed for each of the different types of alternative options (to the current KID) proposed by the ESAs. Section 12 sets out the associated draft legislative amendments that would be needed for each of these options.

[10] Commission Regulation (EU) No 583/2010 of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of a website, OJ L 176, 10.7.2010, p. 1.

[11] JC 2019 55

5. Future performance scenarios

5.1 Background

The PRIIPs Regulation requires PRIIP manufacturers to include appropriate performance scenarios and information about the assumptions made to produce the scenarios in the KID. The current PRIIPs Delegated Regulation sets out how this is to be done. For most PRIIPs[12] the prescribed methodology requires an illustration of how the PRIIP could perform according to four different scenarios (stress, unfavourable, moderate and favourable). The figures presented in these scenarios are generally derived from a model which simulates possible outcomes based on the returns or prices, and fluctuations in those returns, over the previous 5 years.

In summary:

- The unfavourable, moderate and favourable scenarios reflect the 10th, 50th and 90th percentiles of the estimated distribution of future returns respectively[13];
- The stress scenario is calculated using different parameters with a view to estimate a worst-case scenario. It recognizes that while a total loss of investment could happen, it is extremely unlikely for most PRIIPs that have a summary risk rating of less than 7.

In the November 2018 CP the ESAs discussed the concerns that had been expressed by stakeholders, that the existing performance scenarios risk providing retail investors with inappropriate expectations about the possible returns they may receive. This is because the current methodology is pro-cyclical in nature. The methodology generates outcomes with high returns when the product has experienced high returns over the previous five years, and will generate lower returns when the opposite is true. However, in reality, periods of high returns are generally followed by periods of low returns and vice versa.

The PRIIPs Regulation came into force during a period of high growth where, for example, some funds had generated returns of over 20% per year. In some cases, the performance scenarios have also shown an expectation of having a positive return for the unfavourable scenario[14]. There have also been cases of favourable scenarios for a product showing potential returns that are greater than any returns ever observed for that product.

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[12] There is an exception, for example, for options and futures traded on a regulated market to present performance in the form of a pay-off structure graph (Article 3(5) of the PRIIPs Delegated Regulation).

[13] Future outcomes are impossible to predict. However, a model of how prices evolve in a financial market can be used to estimate the distribution of returns accessible to the investor. The methodology for performance scenarios assumes that the model results in the distribution of returns for the PRIIP (or the assets underlying the PRIIP) observed over the past 5 years. The historical distribution of returns is used to estimate the distribution of returns of the PRIIP at the end of the recommended holding period. The 10th, 50th and 90th percentile returns are read from this estimated distribution.

[14] This means that it is estimated that 90% of the time the investor would have a positive return. This has been a particular issue for interest rate products where US interest rates tripled over the past 5 years.

During the targeted review of the PRIIPs Regulation carried out at the end of 2018, given the scale of the changes required and the limited timeframe available, the Final Report deferred proposals to change the methodology or presentation of performance information.

This consultation paper presents the ESAs proposals following our further work on this topic.

5.2 Probabilistic performance scenarios – work to revise the methodology

Despite the shortcomings described above, the current methodology for probabilistic scenarios has a number of advantages. It is based on a simplistic model which allows investors to compare all products on the basis of what they may expect to receive using specific numbers that are generated in a consistent and prescribed way for the vast majority of PRIIPs. Because it is based on actual observed historical returns, it does not require PRIIP manufacturers to use or create complex models to either, extract values to be used in estimating the distribution of returns, or to construct an estimated distribution of returns.

Respondents to the November 2018 CP were of the view that it is important to change the underlying methodology to address the problem of pro-cyclicality and the potentially misleading estimates of favourable and unfavourable returns.

Alternative probabilistic approaches and their presentation were discussed in that consultation paper. The proposed changes to the methodology included the use of risk-neutral expectations as an anchor point for the scenarios or extending the historical period used to measure performance to 10 years. Extending the historical period does not eliminate the problem of pro-cyclicality, however, and is not considered in this paper. Some respondents indicated that the use of risk-free rates may have merit if risk premia were included. This consultation paper explores how risk premia could be defined.

The proposed amendment to the current methodology is therefore to change the estimator of the growth rate so that the observed historic growth of the asset is no longer used.

Based on some recent academic studies, the ESAs have focused their analysis on the use of dividend rates or yields to estimate asset specific risk premia and have developed a revised methodology based on this.

According to this methodology, the expected growth rate for a particular asset will be the sum of a reference rate common to all asset types and an asset specific risk premium. The details of this methodology and its application to different types of PRIIPs is explained in Section 5.4. The associated draft RTS amendments to the PRIIPs Delegated Regulation are shown in Section 12.1.

The ESAs have carried out several studies to assess this approach. In one study, the revised methodology was applied to all products tested during the development of the original RTS. This allowed us to check the impact of this methodology against results that validated the original methodology. A second study applied the revised methodology to funds with high historical returns in the past five years to ensure the methodology does not suffer from pro-cyclicality. A third study specifically looked at the ability of the methodology to generate scenarios for real estate funds and assess the reasonableness of the results. The final study was to assess the methodology by comparing generated scenarios against actual returns over a long time span (investment products which have a price history of at least 30 years).

The results of these studies suggest that the proposed methodology can be applied to a number of different types of PRIIPs, gives meaningful results, and does not experience pro-cyclicality.

However, given the wide scope of the Regulation, it has not been possible to test the approach on the full range of different types of PRIIPs. We have therefore not been able to establish whether:

- the methodology is straightforward to implement for all PRIIPs;
- the methodology gives reasonable results for all PRIIPs.

It is essential that the methodology is meaningfully tested against a comprehensive range of PRIIPs. The ESAs will therefore continue their efforts in this regard before modifications to the methodology are proposed to the European Commission. Significant contributions from industry stakeholders will be important to ensure the meaningfulness of the testing. The ESAs will organise discussions with stakeholders to ensure testing is performed in a consistent manner across a wide range of PRIIPs.

At the same time, the ESAs remain open to consider alternative options. Section 5.7 seeks feedback on some possible alternative approaches, including based on specific proposals received already from external stakeholders. The ESAs will also consider any alternative options that respondents to this consultation would put forward.

5.3 Impact of changes in the presentation of probabilistic performance scenarios on the methodology

As discussed in Section 4, the ESAs are considering removing intermediate scenarios and the stress scenario from the future performance scenarios. The ESAs have received feedback that the existing performance scenarios provide an overload of information and should be simplified.

The presence of intermediate and stress scenarios also raises significant challenges regarding the formulation of the RTS that prescribe the methodology.

- The ESAs are aware of specific issues for Category 3 PRIIPs, where the methodology for the calculation of intermediate scenarios is not specified in detail. For example, Category 3 PRIIPs require 100 million Monte Carlo simulations to properly determine one intermediate scenario (as opposed to 10,000 for one scenario at the end of the recommended holding period).
- The specification of the stress scenario at the end of the recommended holding period in the current methodology requires the use of a growth rate of zero and a higher value of volatility

based on the distribution of historical volatility measured over pre-defined intervals observed in the past 5 years. The ESAs note that the calculated yield on some assets is currently negative.

On the other hand, the intermediate scenarios can be seen as relevant to indicate the implications of ending the investment before the end of the recommended holding period, including any exit penalties, as well as how the performance of the product can evolve over time.

Given the possibility that these scenarios are removed, they are not included at this stage in the new version of the future performance scenario methodology (i.e. draft RTS). However, the ESAs would be interested in the views of stakeholders on the proposed approach, and if the intermediate and stress scenarios were to be kept, how the requirements should be drafted.

In addition, if the intermediate performance scenarios are eliminated from the performance section of the KID, an assumption of performance at an intermediate point may still be needed for the 'What are the costs?' section.

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

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

5.4 Explanation of proposed dividend yield methodology for probabilistic performance scenarios

This section provides some additional explanation of the revised methodology using dividend yields to estimate future growth rates. It explains the assumptions underlying the methodology, the choice of parameters to implement it, and how the methodology works for different types of PRIIPs. There is an open question regarding exactly what should be prescribed in the RTS (level 2) and what should be recommended in level 3 guidance (Q&A) produced by the ESAs.

The methodology for calculating probabilistic performance scenarios is based on the following assumptions:

- The expected return distribution for a PRIIP (or the assets underlying) can be approximated by a log-normal distribution[15]. A better estimate of a return distribution is given by a Cornish-

[15] The Pricing of Options and Corporate Liabilities (Black and Scholes) – The Journal of Political Economy, Vol. 81, No. 3 (May Jun, 1973), pp. 637-654.

Fisher[16] expansion of a log-normal distribution which replicates the wider tails and narrower peaks seen in market studies.

- Riskier assets will have a higher expected return (referred to as the risk premium).
- The long term variability of asset performance is stable (certainly when considering holding periods greater than 5 years) and can be estimated using historical data.

The methodology consists of two elements: the estimation of the parameters used in estimating the return distribution, and the calculation of the quantiles of the return distribution. The methodology differs for three types of PRIIPs to ensure that the complexity of the calculation matches the complexity of the product. The three broad classes of products are:

- Funds and fund-like products which are purchased at a single point in time; and
- Funds and fund-like products where the investment accrues over time (e.g. regular premium insurance-based investment products); and
- Structured products and other structures where the pay-off profile is discontinuous or depends on distinct events over the life of the product[17].

Funds and fund-like products can be thought of as a collection of assets where the performance of the product is the sum of the performance of the individual components.

The performance of structured products reflects the application of a formula and/or terms that define the performance of the product in respect of the observed price history of its underlying assets.

The calculation of the expected return is common to all three classes of products. The expected return of an asset is given by the sum of a reference rate and an asset specific risk premium. The reference rate for an asset is given by the interest rate curve derived from sovereign bond prices of the country of the asset. This ensures that the country-specific risk is captured. The asset-specific risk premium for different types of assets is given by:

- Equity instruments: Dividend rate (and all other distributions, including share buybacks) received by the end investor in the PRIIP;

- Bond instruments: Coupon rates less the reference rate

- Fx instruments: Expected forward rate less the reference rate

- Commodities: Expected forward rate less the reference rate

- Real-estate funds which invest in property: the asset-specific risk premium is given by the dividend rate.

[16] There are a number of functions which describe the probability of finding a particular value in a limited range, of which the log-normal distribution is one such function. The Cornish-Fisher expansion corrects the log-normal distribution to replicate the exact properties of a distribution observed in the real world.

[17] For PRIIPs, there are however, four defined product Categories. In summary: Category 1 PRIIPs are derivatives or derivative type instruments where there could be a substantial likelihood of losing all one's investment; Category 2 PRIIPs are funds and fund-like vehicles which have a linear dependence on the price of shares or bonds; Category 3 PRIIPs are structured products which have a non-linear dependence on the price of shares, equity index levels, bond prices, interest rate levels, FX rates, commodity prices or other prices or levels that are publicly observed; Category 4 PRIIPs are products that depend in part on factors not observed in the market.

Where there is no expected forward rate; or no expected cash distribution; or the purchaser of the PRIIP does not receive the dividend, cash disbursement or coupon: the asset-specific risk premium is zero.

The proposal to use the dividend rate and all other distributions to the holder of the PRIIPs is based on academic evidence. In particular, we note the following quote from John Cochrane's Presidential Address to the American Finance Association[18]:

In each case our view of the facts has changed completely since the 1970s.

- *Stocks. Dividend yields forecast returns, not dividend growth.*
- *Treasuries. A rising yield curve signals better 1-year returns for long-term bonds, not higher future interest rates. Fed fund futures signal returns, not changes in the fund rate.*
- *Bonds. Much variation in credit spreads over time and across firms or categories signals returns, not default probabilities.*
- *Foreign Exchange. International interest rate spreads signal returns, not exchange rate depreciation.*
- *Sovereign Debt. High levels of sovereign or foreign debt signal low returns, not higher government or trade surpluses.*
- *Houses. High price/rent ratios signal low returns, not rising rents or prices that rise forever.*

The methodology assumes that PRIIPs which deliver equity dividends to the holder of the PRIIP are primarily funds and fund-like products. The methodology proposes that the expected risk premium attributable to the equity component of a fund is based on the average dividend yield paid to the PRIIP and attributable to the holder of the PRIIP. To calculate this average dividend yield the methodology proposes that manufacturers use the average dividend yield for each country/sector represented in the fund weighted by its representation in the fund.

The methodology assumes that other classes of assets, such as government bonds, corporate bonds and foreign exchange instruments, would be treated in a similar manner as equities.

The remaining parameters needed for the calculation are the variance, skew and excess kurtosis of the return distribution. These parameters are obtained from the 5-year history of daily returns of the PRIIP for funds and fund-like products; or from the 5-year history of daily returns of the assets underlying the PRIIP (structured products).

For funds and fund-like products the variance, skew and excess kurtosis are directly calculated and used in the Cornish-Fisher expansion.

For funds which are purchased at a single point in time, the quantiles are obtained directly from the Cornish-Fisher expansion.

[18] Presidential Address: Discount Rates, John Cochrane, The Journal of Finance, Vol. 66 No. 4, August 2011.

For funds where the invested amount accrues over time, the quantiles are obtained from a Monte Carlo generated return distribution. Each Monte Carlo path is generated by obtaining a simulated return for each period in the recommended holding period using the Cornish-Fisher expansion.

For structured products, the quantiles are obtained from a Monte Carlo generated return distribution. The inputs to the Monte Carlo procedure are the 5-year history of daily returns of each asset. Each 5-year history is shifted by a constant amount to ensure that the distribution has the correct expected return. A single price path is constructed by selecting a random return from the sample for each day in the recommended holding period.

Testing the methodology on money market funds (see next Section 5.5) suggests that the volatility of historical daily returns does not provide a good estimate of the variance of returns over a longer time frame. A better estimate of the observed variance over longer holding periods for EUR denominated money-market funds is provided by the implied volatility of options on BUND futures. The fundamental reason is that changes to the overnight rate paid by the central bank change infrequently but in large increments (typically 0.25%). Options with a maturity of 1-year or greater have to capture these potential changes; daily changes in the overnight rate are minimal on the vast majority of trading days.

For this reason, the draft RTS in Section 12.1 includes a specific treatment for the specification of the volatility of money-market funds.

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

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

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

12. **How should share buyback rates be estimated?**

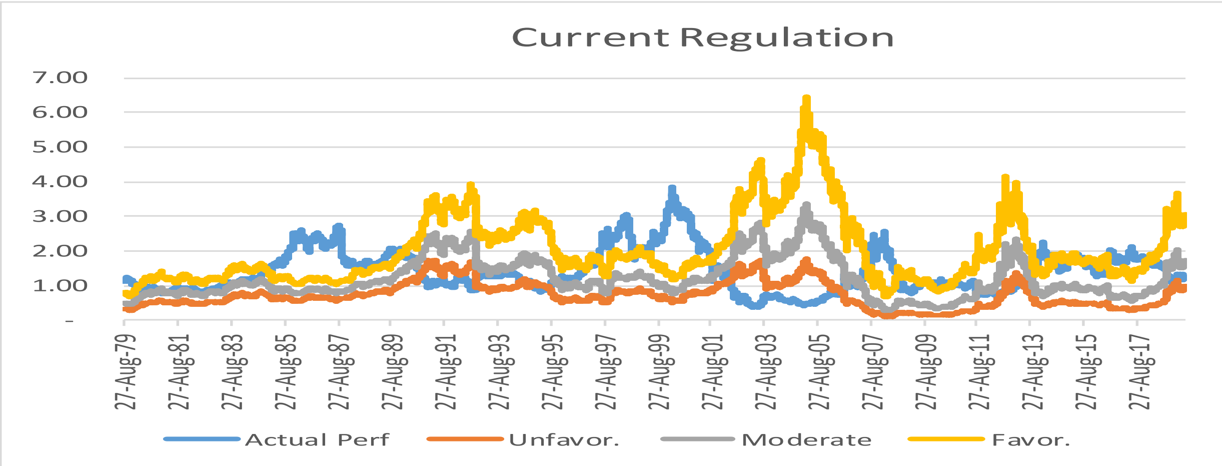
13. **Do you agree with the approach for money-market funds? Are there other assets which may require a similar specific provisions?**

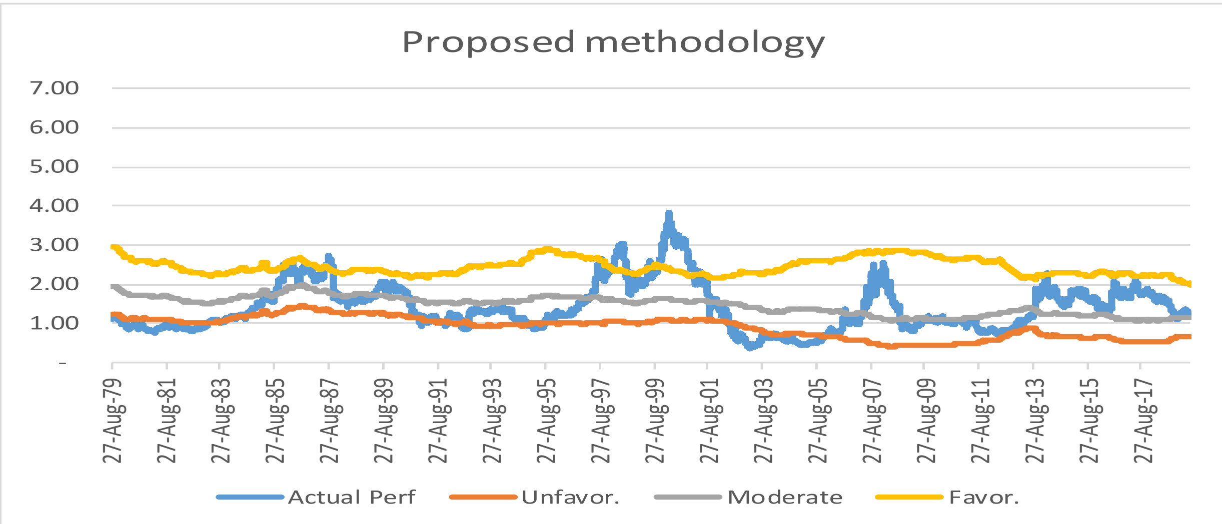
14. **The methodology proposes that the future variance be estimated from the 5-year history of daily returns. Should the volatility implied by option prices be used instead? If so, what estimate should be used if option prices are not available for a particular asset (equities namely)?**

5.5 Evidence so far for the dividend yield methodology

5.5.1 Example: Broad Based Large-Cap German Equity Fund

The following graphs show the scenarios constructed using both the current methodology and the proposed revised methodology together with the observed returns using the date range for which historical prices are available. The recommended holding period is assumed to be 5 years which means the period shown in the figures is 10 years shorter than the period for which prices are available.





It is clear from the figures that pro-cyclicality is no longer an issue. The following table gives the percentage of time that the actual performance is below the indicated scenario.

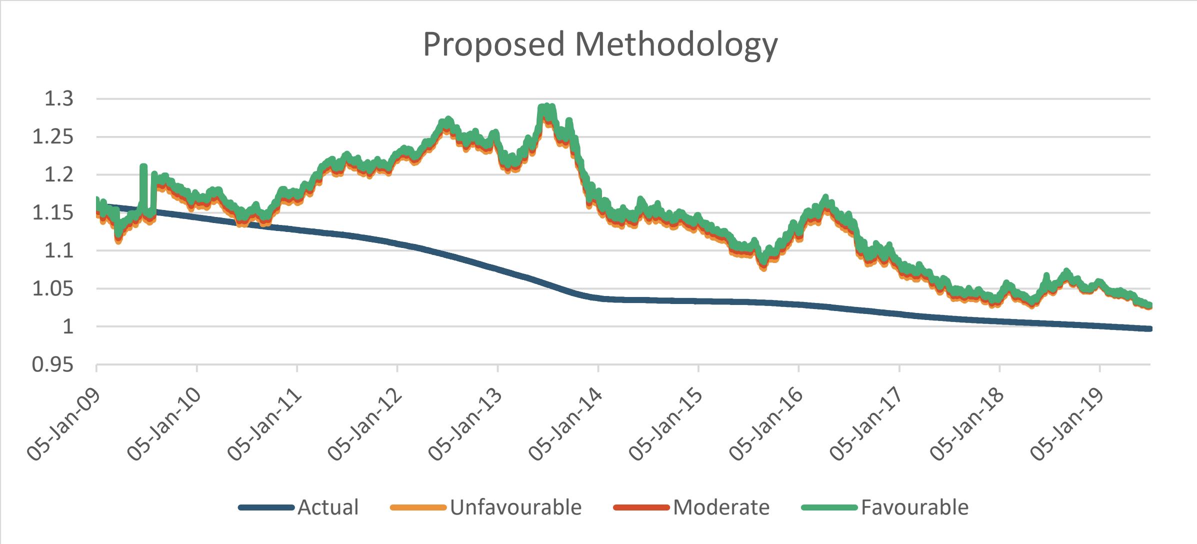
Scenario	Expected percentage	Current Methodology	Proposed Methodology
Percentage of time below unfavourable scenario	10%	20%	22%
Percentage of time below/above moderate scenario	50%/50%	34%/66%	61%/39%
Percentage of time above favourable scenario	10%	36%	6%
Correlation between moderate scenario and actual performance	100% (if perfect)	-40%	50%

The above table shows that the proposed methodology, whilst not perfect, is an improvement on the current methodology. Importantly, the correlation between the moderate scenario and the actual performance is 50% - which suggests that the method explains approximately 25% of the variance in actual returns. The measured quantiles are closer to the expected quantiles based on the percentage of time that the fund is below the unfavourable scenario or above the favourable scenario. The principal reasons for the higher-than-expected percentage of returns below the unfavourable scenario (for both the current methodology and the proposed methodology) are the oil crisis in the mid-1970s and the slump in returns following the technology boom in the late 1990s, both of which were unexpected.

The principal reason that the current methodology results in a high percentage of returns exceeding the favourable scenario is pro-cyclicality. It is clear that this feature disappears with the proposed revised methodology.

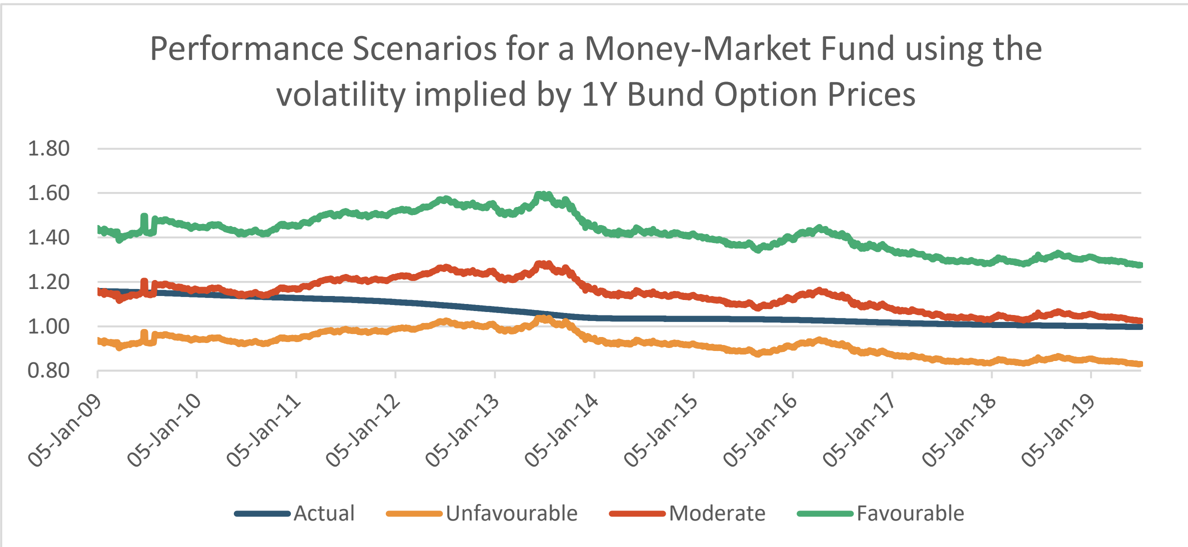
5.5.2 Example: Money-market Fund

The following plot is similar to the plots shown above using the proposed methodology. The fund is a French money-market fund. The recommended holding period is again 5 years.



The plot illustrates the difficulty of constructing a reasonable range of outcomes for money market funds using historical volatility. Money market funds have a very low volatility that is not representative of the volatility of the underlying interest rate which determines the return. In a falling interest rate environment, as is the case for most of the period 2005-2014, the observed return will always be below the unfavourable scenario.

The following plot shows performance scenarios constructed assuming an annualized volatility consistent with the average implied volatility of options on the German Bund Futures. From this plot it is clear that the observed performance never exceeds either the unfavourable scenario (rates moving down) or the favourable scenario (if rates were to move up).



5.5.3 Structured Products

During the development of the current PRIIPs Delegated Regulation, 63 different structured payoffs were tested. Repeating the tests using the proposed methodology resulted in largely similar results.

5.6 Compensatory mechanism to address potential methodological faults

Notwithstanding the work we have done to correct for the issues identified with the current methodology for producing probabilistic performance scenarios, there is always the possibility that issues will arise in the future with the changes to the methodology proposed in this consultation paper. Without comprehensive testing of all product types in all possible market conditions, we cannot conclude definitively that issues will not arise with the proposed methodology.

The ESAs are therefore of the view that in addition to reviewing the methodology for producing probabilistic performance scenarios, compensatory mechanisms might well prove to be needed. These could include for example:

- lowering the favourable scenario to match the maximum return observed in the past if the performance in the favourable scenario is higher than any return observed in the past;
- raising the unfavourable scenario to match the minimum return observed in the past if the performance in the unfavourable scenario is lower than any return observed in the past;
- lowering the unfavourable scenario to match the manufacturer's expectation of an unfavourable outcome, if the unfavourable scenario is considered to be unrealistic.

For the first two options, the "past" could be defined with reference to the existing data history requirements in the PRIIPs Delegated Regulation (Annex II, Part 1, points 5 and 6) or alternatively a longer minimum period of time could be used.

The latter option based on the manufacturer's expectations has been considered in the past, but was found to be problematic due the goal of PRIIPs to provide comparable information for all products to potential investors.

Another possibility would be to define upfront caps or limits on the level of performance that can be shown, although there are challenges to appropriately define such caps and they may need to be regularly reviewed[19]. This approach could be applied in different ways, but it would seem to be necessary to at least distinguish between different broad asset classes (e.g. set a maximum limit for equities, bonds, etc.):

[19] It is acknowledged that such a mechanism has similarities to the possible alternative methodology to set maximum growth rates per asset class described in Section 5.7 below.

- The aim could be to lie relatively close (i.e. above) to long-term averages, or alternatively to capture an upper bound of reasonableness, i.e. lying on the higher level of what has been observed historically;

- Separate limits could be defined for each of the scenarios

Given the relevancy and materiality of this issue, ESAs are in particular seeking feedback from stakeholders on these options for compensatory mechanisms. The ESAs would also welcome any other specific proposals of compensatory mechanisms, if possible supported by evidence of their relevance based on results of testing the revised methodology:

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

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

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

5.7 Other probabilistic methodological approaches

While the ESAs believe the decomposition of growth rates into a country specific reference rate and asset specific risk premium (as detailed in Section 5.2 and further in Section 5.5 above), could provide a relevant predictor of expected returns, as well as flexibility to adapt to regional divergences, the ESAs also acknowledge that such a methodology is relatively complex and may present challenges, both in terms of implementation by the industry, and explanation to consumers. This would be particularly relevant for multi-asset portfolios, where the underlying investments are based in several different countries. The ESAs are therefore of the view that while this option is viable, better alternatives could still be envisaged. Some of these other options are detailed below, but the ESAs would be open to new proposals presented by stakeholders.

While it is important to appropriately differentiate growth rates by asset, the ESAs acknowledge the inherent uncertainty in any future growth assumptions. The ESAs are therefore considering possible simplified alternatives and are interested in stakeholders’ views on these types of approaches.

One such approach would be to set prescribed maximum growth rates determined solely by asset class, such as:

Asset class	Maximum growth rate
Equities	A%
Property	B%
Bonds	C%
Cash	D%
Hybrid/ Complex	E%

In the above table, rates would be rounded to a single decimal place (possibly limited to 50 bps increments). Such an approach would be simpler to both implement and communicate to consumers, and would remove the primary concern with the current methodology; specifically unrealistically favourable growth rates.

In order to populate the table, a clear methodology for the calculation of the rates would be necessary, with a possible approach being to base them on an analysis of relevant European data over the past 40 years. While the potential organisational challenges of such a process are still to be assessed, a supervisory or external body could assume responsibility for the calculation, and regular review, of the rates within the above table.

A drawback with this approach is that the same maximum growth rate would apply to all investments within a particular asset class, and no distinction would apply by country. While acknowledging this possible deficiency, the ESAs are interested in feedback on whether the increased simplicity and transparency associated with such an approach justifies this change.

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

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

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

During the development of this consultation paper, the ESAs also received several specific proposals from different stakeholders for other approaches to address the pro-cyclicality of the current methodology. These approaches were all loosely based on the Capital Asset Pricing Model (CAPM) that was developed by academics in the 1950s.

In general terms, the alternative options raised so far include:

a) a model where the expected return for an equity asset is given by the long-term return of a world equity index adjusted by the Beta of the specific equity name (with the expected return for other assets given by forward prices observed in the market);

b) a proposal to use volatility based risk premia. The risk premium would depend on the Sharpe ratio for each asset class or fund class and the asset or fund specific volatility. The Sharpe ratio for each asset class or fund class could be derived using historic averages;

c) a proposal to use fixed risk premia for equities derived e.g. from long term historical data. The approach could be extended to a restricted list of asset classes.

Option (a) is based on the Capital Asset Pricing Model (CAPM) that was developed by academics in the 1950s. It is considered to raise some challenges in terms of complexity of implementation. In option (b) and (c), the risk premia together with an appropriate reference rates results in the expected growth rate.

Based on the academic evidence[20] that the best predictor of equity risk premia is the expected dividend rate, and the testing conducted so far (for example as described in Section 5.6), at this stage the ESAs are of the view that the approach described in Section 5.2 is preferable, subject to the outcome of the further work to test this methodology.

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

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

[20] Damodaran, Aswath, Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2016 Edition (March 5, 2016). Available at SSRN: https://ssrn.com/abstract=2742186 or http://dx.doi.org/10.2139/ssrn.2742186

6. Alternative approach to performance scenarios - use of illustrative scenarios

6.1.1 Structured products – option of only showing illustrative scenarios

When submitting the proposed options for consumer testing to the European Commission the Joint Committee of the Chairs of the ESAs wrote a letter[21] explaining that illustrative scenarios, similar to the approach that is currently used for so-called structured UCITS,:

> *may provide more meaningful information for structured products [than the approach currently used for the KID], as it is very challenging to define a revised methodology that adequately fits structured products without risking inappropriate results. It appears evident that the critical factor in understanding the future performance of a Structured product is understanding how the formulae determining pay offs is sensitive to different underlying factors, as determined by the combination of elements that make up the structured instrument*

On the other hand, the main disadvantage of this approach is the discretion of the manufacturer to select the scenarios and the potential impact on the ability of the investor to compare among different PRIIPs when using this type of approach.

Taking into account the objective of comparability, the ESAs also proposed to test combining illustrative scenarios with probabilistic performance scenarios. However, such a combination seems to have the potential to result in overlapping information and a potential overload of information to the investor.

In view of this, although the Commission have decided not to test the option of including only illustrative scenarios for structured products, the ESAs have still included this option in this consultation paper for stakeholder feedback, as well as the option of combining illustrative and probabilistic performance scenarios.

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

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

6.1.2 Structured products – scope and methodology

The ESAs would propose to use the definition of Category 3 PRIIPs as specified in point 6 of Annex II of the PRIIPs Delegated Regulation to define the scope of PRIIPs to which the requirement to show

[21] JC 2019 46

illustrative performance scenarios would apply. This maintains the current logic of the PRIIPs Delegated Regulation in terms of applying the same methodology to PRIIPs that are "non-linear".

This means that certain types of PRIIPs (for example certain types of derivatives or credit-linked notes), which do not strictly correspond to the definition of structured products as they are commonly referred to, would fall into the scope.

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

Given the longstanding application of Article 36 of the UCITS Regulation 583/2010 and the inclusion of such scenarios in the KII Document, these requirements have been taken as a basis. However, several adjustments are considered to be necessary:

- A specification regarding the costs to be taken into account. Most of the costs of structured products are implicit or indirect, in the sense that they are included in the nominal value. As illustrations are expected to be based on the nominal value, the returns shown would be, by definition, net of costs. However, in certain cases entry costs are charged by the issuer or distributor on top of the nominal value. It is therefore considered necessary to add a provision that states that the returns presented in the illustrations should be net of costs. This also reflects the comparable provision for probabilistic performance scenarios (currently point 31 of Annex IV of the PRIIPs Delegated Regulation);

- To prescribe certain narratives to be used to explain the nature of the scenarios. This follows the current approach in the PRIIPs KID that, as far as possible, a standardised template should be used.

The draft legislative requirements are included in Sections 12.2 and 12.3.

6.1.3 Insurance-based investment products

For insurance-based investment products, the ESAs proposed to test an option involving the inclusion of illustrative type scenarios, as well as probabilistic scenarios (see Option 5 of the ESAs consumer testing proposals). However, in view of the concerns of the European Commission regarding the practical feasibility of this option, the ESAs do not consider this as a sufficiently high priority to further pursue during this review. In particular, the ESAs took into account:

- The concerns of the European Commission regarding the length of this option;

- The absence of an existing EU framework to use as a basis for such approaches;

- While the ESAs had considered it relevant to use the opportunity of the consumer testing to gather feedback from consumers on how they respond to such approaches, they are not considered to be essential to respond to the criticisms of the current methodology.

7. Inclusion of information on past performance

The inclusion of information on past performance in the KID was discussed in the November 2018 CP, and in the February 2019 Final Report the ESAs stated:

> *the ESAs intend to consider further in the context of their upcoming work (see also Section 5) if and how information on past performance could be included in the PRIIPs KID and for exactly which types of PRIIPs. This work would be with a view to the amendments needed in relation to the potential inclusion of UCITS within the scope of PRIIPs at a later stage. The ESAs will also consider if there are synergies in relation to the ongoing work to report on the costs and past performance of retail investment products. In relation to insurance-based investment products, for example, where respondents to the CP highlighted challenges to present information on past performance, or to do so using the approach in the KIID, EIOPA recently stated that it will work further during 2019 "on developing its methodology and approach" to identify and report on past performance in order to have complete and consistent data, with a view to ensuring the significance of the analysis*[22]*. This applies, in particular, for products which distribute a portion of the PRIIP manufacturer's profits to retail investors (e.g. "profit-participation").*

Taking into account the feedback from the November 2018 CP[23], the ESAs do not propose to require the inclusion of past performance for Category 1 or Category 3 PRIIPs and therefore the inclusion of past performance for these types of PRIIPs is not part of the consumer testing exercise.

The ESAs also did not propose to test an option of only showing past performance (and not future performance scenarios) for certain types of PRIIPs. This reflected the fact that a consumer testing for presenting (only) past performance was already conducted when developing the current requirements for the UCITS KII document. The ESAs also took into account that showing only past performance may not be in line with the current PRIIPs Regulation. The consumer testing will therefore assess the effectiveness of showing past performance information together with future performance scenarios.

Sections 12.4 and 12.5 sets out proposed rules for the inclusion of past performance for certain types of funds and insurance-based investment products. Subject to the results of the consumer testing and the feedback to this consultation, the ESAs will decide on their final recommendations. At this stage, the proposals cover the inclusion in the KID of past performance for linear PRIIPs (AIFs, UCITS and unit linked insurance-based investment products) and for linear investment options (AIFs, UCITs, internal insurance funds).

[22] EIOPA: First Report Costs and Past Performance (December 2018), page 36.

[23] See page 7 – "Where past performance would need to be simulated (e.g. structured funds, structured products and derivatives), it was stated that this would raise significant technical challenges (e.g. availability of data), that it would not provide meaningful or comparable information to investors, and that it could create adverse incentives for example to design products that would have more favourable simulated past performance"

For other types of insurance-based investment products, in particular products which distribute a portion of the PRIIP manufacturer's profits to retail investors (e.g. “profit-participation”), the ESAs are of the view that increased transparency regarding past performance should be aimed for, but a sound methodology is not available at this stage. Therefore, the proposals in this consultation paper do not cover these types of PRIIP. As stated in the February 2019 Final Report, there is a link to the ongoing work to report on costs and past performance of retail investment products. However, before past performance information can be included in the KID for these types of PRIIPs, it is necessary for there to be a consistent methodology to identify and report past performance, in order to ensure the meaningfulness of the information. It is aimed to develop such a methodology as part of EIOPA’s work to report on the costs and past performance of insurance-based investment products. However, this work is still ongoing and may not be completed and adequately tested until after Q1 2020. The ESAs, therefore, intend to review this issue in a next step with a view to also including past performance in the KID for other types of insurance-based investment products, taking into account the progress made in the context of the work to report on the costs and past performance of retail investment products.

Furthermore, the ESAs noted that in their responses to November 2018 CP, various stakeholders expressed concerns that it would not be possible to meet the requirement in Article 6(4) of the PRIIPs Regulation that limits the length of the KID to 3 sides of A4. The ESAs are considering whether this would be a relevant point to recommend a specific change to the PRIIPs Regulation.

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

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

As stated above, the proposals for consumer testing submitted by the ESAs contain several different ways to present past performance information for insurance-based investment products. Draft rules for these approaches are included in this consultation paper for feedback from stakeholders, as follows:

- The rules from the UCITS Regulation 583/2010 including the established presentation of past performance as a bar chart have been adapted so that they could apply to all types of linear funds and insurance-based investment products;

- Draft rules have not been developed at this stage for a “3 element”[24] past performance bar chart (i.e. including investment returns and bonuses paid out in separate columns), given that this option is only considered to be relevant for Category 4 PRIIPs and it is not recommended to include past performance for these types of products during this review;

- Although the Commission have decided not to test the option of showing average past performance, since the ESAs are of the view that this is a relevant means of communicating past performance for longer term products, this option is included in this consultation paper for stakeholder feedback. The ESAs are therefore interested in feedback on whether this display of past performance is preferred for certain types of PRIIPs, and in particular if it should

[24] See Option 3 for insurance-based investment products of the ESA consumer testing proposals

only be applied where the recommended holding period is of a certain minimum duration (e.g. 10 years).

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

Regarding the adjustments to the rules taken from the UCITS Regulation 583/2010, the ESAs would be interested, in particular, in stakeholders' views on the following aspects:

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

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

31. Do you see merit in further specifying the cases where the UCITS/AIF should be considered as being managed in reference to a benchmark, taking into account the provisions of the ESMA Questions and Answers on the application of the UCITS Directive[25]?

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

[25] See "Section II – Key Investor Information Document (KIID) for UCITS" (in particular, Q&A 8) of the Q&A document available at: https://www.esma.europa.eu/sites/default/files/library/esma34-43-392_qa_ucits_directive.pdf

8. Costs

8.1 Introduction

This Section presents some alternative options to amend the rules associated with Article 5 of the PRIIPs Delegated Regulation (in the corresponding Annexes) which address the methodology to identify and calculate the costs of PRIIPs and how these should be presented in the section of the KID 'What are the costs?'. The ESAs' work on this topic follows their statement in the February 2019 Final Report that this was a priority area for this review:

> *based on the feedback provided to the CP, as well as other information gathered by the ESAs following the implementation of the KID, it is intended to examine whether the methodologies to calculate, and the approach to present, costs, are achieving the intended outcomes in terms of capturing all products costs and facilitating comparability, as well as the interaction with other legislation, in particular MiFID II and IDD. The expected focus of this analysis would be the transaction cost methodology and the reduction in yield (RIY) approach.*

8.2 Methodology and presentation of costs and summary cost indicators (except transaction costs)

8.2.1 Current approach

Information on costs is currently presented in the form of two separate tables. The first Table 1 (costs over time) shows the total or aggregated costs that are expected to be paid depending on the investment being held for different time periods and how these total costs impact on the investor's return. The second Table 2 (composition of costs) shows a breakdown of different types of costs, including one-off costs and ongoing costs, and how each of these different costs impacts on the return per year assuming that the investment is held until the recommended holding period.

These cost tables use a reduction in yield (RIY) measure as the cost indicator as a way of showing how the costs taken or incurred at different times during the investment period affect the return achieved by the retail investor. The RIY is calculated by comparing a notional gross yield for a product (i.e. the return that would have been achieved if there had been no costs) with the return achieved taking into account those costs. This cost measure is applied to all types of investment products within the scope of PRIIPs and therefore aims to effectively facilitate comparison.

8.2.2 Issues raised by stakeholders

Since the implementation of PRIIPs, concerns have been raised by stakeholders both regarding the overall approach to use RIY as the cost indicator, as well as regarding specific aspects of the cost presentation. Regarding the RIY, it is argued that it is not well understood by retail investors, in particular for non-insurance PRIIPs (i.e. PRIPs), for which there is more experience with other cost indicators. Related to this, while RIY figures could be used to comply with requirements in MiFID II[26] or IDD[27], distributors of MiFID products use a different figure as the cost indicator (total costs over investment), and show the impact on return separately, illustrating this in different ways as a methodology is not mandated. It has been commented that this inconsistency between the application of the different legislative frameworks creates confusion amongst retail investors and advisors.

In terms of the more specific issues, some of the points that have been raised by stakeholders include:

- In order to calculate the RIY cost figure it is necessary to make several assumptions regarding the investment return that the PRIIP will achieve and the amount invested by the investor. These assumptions are necessary for methodological reasons in order to show the effect of aggregate costs, but by their nature do not reflect the actual situation of individual investors, such that it could lead to possible misunderstanding on their part. For most PRIIPs, it is required to use the return that would be achieved based on the moderate performance scenario. However, this assumption is not stated in the KID, and some stakeholders have seen this as a significant omission.

- Some of the terminology used or prescribed narrative texts are not appropriate for some types of PRIIPs.

- For Table 1, it may not be necessary to show costs at three different time periods and that this contributes to an overload of information for the investor.

- Regarding Table 2, the same assumptions of expected return and initial investment amount need to be made, but are not disclosed. In addition, since this Table shows costs on the basis that the product is held for the recommended holding period, this can obscure the nature of the entry and exit costs. More specifically:
    - The percentage figure shown in Table 2 shows the impact of the entry costs per year. This means that, for example, a 4% entry fee taken from the amount invested will be shown as a lower percentage in the KID. This is because such an entry cost is only applied at one point in time, and so has a lower annual impact when looking over the whole investment period. It has been argued that some retail investors are familiar with entry costs being presented as a percentage of the amount invested so may misconstrue the figure in the KID.

[26] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, OJ L173, 12.6.2014, p. 349

[27] Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution, OJ L26, 2.2.2016, p.19

- While there is a separate section in the KID where early exit penalties have to be clearly disclosed[28], and it is explained in the KID that Table 2 reflects the costs at the recommended holding period, concerns have been raised at how investors could misread what is shown. Specifically, if Table 2 shows 0% exit costs, the retail investor could assume that this means that are no exit costs or penalties at any time during the lifetime of the product, which is not necessarily the case.

- The current prescribed narrative text to be used to disclose the nature of any performance fees does not allow the range of different performance fee structures to be appropriately reflected (the ESAs also discussed this concern in the November 2018 CP).

8.2.3 ESA proposals and areas where feedback is requested

The ESAs have assessed these points and intend to make substantive amendments to the Cost Tables. This includes aiming to improve the compatibility with MiFID II disclosures and proposing to require more specific details or descriptions of the main cost types to be disclosed. At this stage, the ESAs have identified a preferred approach, but see value in consulting on a number of different options in order to receive feedback on the preferences of stakeholders between a number of different ways of re-structuring the current Tables.

The ESAs would also like to address a number of issues related to the different options in order to explain the approach proposed or highlight where the ESAs are interested in specific feedback from stakeholders:

- <u>Costs over time</u>. The ESAs consider that it is appropriate to include the costs if the retail investor would exit before the recommended holding period for all PRIIPs with a recommended holding period of over one year. However, it is proposed to change the approach regarding the intermediate or middle time period and the ESAs would be interested in feedback on:

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

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

  - **Applying this approach (i.e. showing also the costs of exit at 5 years) only for PRIIPs with a longer recommended holding period, for example at least 10 years**

  - **For longer term products (e.g. above 15 years) showing exit costs at a different fixed time period (e.g. 10 years instead of 5 years)?**

[28] See Article 6 of PRIIPs Delegated Regulation

- Average annual or total (accumulated) monetary costs – There can be challenges to compare total monetary cost figures for different recommended holding periods. In view of this:

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

- Percentage cost figure

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

- Performance fees and carried interests – The ESAs are considering to combine these two rows in the existing Table 2:

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

- Performance fee narrative - While the ESAs recognise that the current narrative may need to be adjusted, given an ongoing ESMA Consultation paper on Guidelines on performance fees, the ESAs will consider when finalising the RTS, how to extend the existing narrative to all type of performance fee models and not just to benchmark models, based on the outcome of that consultation.

- Treatment of costs disclosures in case of real estate or private equity funds - the current PRIIPs Delegated Regulation does not fully specify the extent to which fees related to the management of the underlying real estate assets, i.e. the properties themselves, should be taken into account in the calculation of the costs indicators. This lack of clarity may decrease comparability between funds offered to investors, depending on the type of funds, but also the Member State in which these funds are marketed. In order to ensure comparability between real estate investment funds and other investment funds, and comparability between disclosure requirements in different Member States, the ESAs are of the view that the disclosure of the costs of real estate or private equity funds should therefore be specified in more details.

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

8.2.4 Preferred and alternative options to restructure the current cost tables

The ESAs consider that it is appropriate to retain some of the main elements of the current approach. In particular, the ESAs continue to be of the view that the RIY is the most pertinent cost indicator for all PRIIPs at the level of overall costs in percentage terms as shown in Table 1. This is considered to allow for a fair and meaningful comparison between all types of cost structures, especially taking into account that the timing at which costs are paid can vary significantly between different types of products.

In view of this, one of the aims of the proposed amendments is to try to ensure that the RIY percentage figures are understood. This includes to disclose the main assumptions upon which the RIY is based, to more clearly separate the RIY (impact on return figure) and the total monetary cost figures (to try to avoid potential confusion as to the interrelation between these figures), as well as to avoid the use of the term "Reduction in Yield" itself and explain the concept differently.

The different options to structure the Cost tables presented by the ESAs are shown in Section 12.6 and are summarized in the Table below.

Option	Main features
Option 1	Revised version of the existing two Tables with a similar overall structure as follows: - For insurance-based investment products the existing approach of showing an RIY cost indicator in Table 2 is kept - For PRIPs, the RIY cost indicator in Table 2 is replaced by a breakdown of the monetary costs if the investor exits after 1 year - In Table 2 a description of the different costs and how they are calculated is added (instead of the current general description of the type of costs).
Option 2	A simpler monetary breakdown of costs is incorporated into Table 1. Table 2 will only include the specific description of the different costs (as in Option 1). Monetary or percentage indicators (e.g. RIY) per type of cost will not be shown in Table 2.
Option 3	Table 1 includes only the RIY figures whereas Total cost figures in monetary amounts are moved to Table 2. Table 2 incorporates the specific description of different costs and how they are calculated (as per Options 1 and 2), but also includes cost indicators in the form of a monetary breakdown of costs at different time periods, as well as total monetary cost figures (as is currently shown in Table 1).

Option 4	A simpler monetary breakdown of costs is incorporated into Table 1 (same as Option 2) Table 2 is removed (in interests of simplification) so there is no description of costs,

The ESAs are of the view that **Option 3 is the preferred approach** to address the issues discussed above. This is based on the fact that it provides a clear split between the percentage RIY based information and the total cost information, and therefore is considered to best provide appropriate alignment with MiFID II disclosures. In addition, while there can be merits to substantially simplify the Tables (i.e. Option 4), some details on the nature of the different cost components are considered relevant to include in the KID and informative both for retail investors, as well as for other parties which use the KID information (e.g. advisors and sellers).

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

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

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

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

8.3 Transaction costs

8.3.1 Current approach

PRIIP manufacturers are required to disclose information on the costs of buying and selling underlying investments of a PRIIP. These transaction costs must include implicit costs, i.e. which are included in the price of a transaction, as well as explicit transaction costs, such as broker commissions or taxes.

When developing this approach the ESAs took into account that the PRIIPs Regulation requires all costs associated with an investment, both direct and indirect costs, to be shown.

There are several different methodologies set out in the PRIIPs Delegated Regulation that need to be followed depending on the nature of the instrument being traded and how long the PRIIP has been operating, and as such how much trading history it has. In summary:

- Where the PRIIP has been operating for at least 3 years, and invests in assets that are sufficiently liquid or traded, the PRIIP manufacturer follows an approach based on "actual transaction costs". These costs are calculated according to a so-called "slippage approach".
- An "estimated costs" methodology. This must be followed for PRIIPs investing in underlying assets other that those described in the bullet point above.

- A "new PRIIPs" methodology. This may be followed where a product has been in operation for less than 3 years.

8.3.2 Issues raised by stakeholders

The focus of discussions and feedback since the implementation of PRIIPs has been on the slippage methodology. The approach in the current PRIIPs Delegated Regulation intends to capture the difference between the price that is actually paid for an asset and the market price that existed at the time that the PRIIP manufacturer decided to transact. It captures the bid-ask spread (i.e. the difference between the price that you can get for selling an instrument compared to the listed price to buy that instrument or vice versa), as well as what is called the market impact - the effect that an order has on the market price during the time that it is in the market, i.e. the time where the transaction is actually being carried out.[29] An assumption of the methodology is that any market fluctuations or volatility while the transaction is taking place are random. The PRIIPs Delegated Regulation requires slippage to be calculated across all transactions for a product over a 3-year period. When slippage is calculated over many transactions, this random element should average out to approximately zero.

Strong concerns have been raised by industry participants regarding the use and implementation of this slippage methodology. These concerns relate to the accuracy and meaningfulness of the results provided.

One of the main criticisms has been that the methodology captures (i.e. records as a cost) market movements that occur while a transaction is taking place, but which are independent of the transaction (i.e. it is argued that this represents market risk rather than a cost to the investor). Linked to this, it has also been emphasized that the methodology can result in negative costs, due to these market movements. The inclusion of negative costs in the KID can be seen as confusing or at least not intuitive to investors.

We also understand that there have been practical challenges relating to the reliability of price data necessary to calculate slippage, in particular for certain Over-The-Counter (OTC) securities, such as bonds or derivatives. Further, there are concerns regarding the extent to which slippage leads to fluctuations in the level of cost disclosure over time.

8.3.3 ESA proposals

The ESAs have assessed carefully the evidence regarding whether the methodology is working as intended and have concluded that some amendments to the current rules are appropriate. The main aspects of these changes are described below:

[29] For example, if a very large order for selling a share or other security is made, the order could result in the market price for that share falls (i.e. the trade results in the market moving against the seller). It can also be noted that an order can be in the market for some time depending on the size of the order and the trading approach (e.g. whether to divide the trade into smaller amounts and trade over time).

- Since implicit transaction costs are an important cost component which have a material impact on investment returns, the ESAs remain of the view that it is very relevant to provide, whenever possible, transparency on such costs to investors. This should also promote effective competition within the market in order to encourage manufacturers to trade in a way that is in their investors' best interests, and in particular to minimize such costs;
- At the same time, there needs to be a high level of assurance that the figures shown in the KID are an accurate reflection of the actual costs incurred. In particular, the ESAs recognize that currently the amount of explicit transactions paid by investors are not comprehensively reflected, as a result of the requirement to use the slippage methodology. Further, taking into account the experience of how the methodology works in practice for different types of assets, it is relevant to adjust the approach, in particular for OTC transactions and those involving non-financial or real assets;
- The methodology needs to be proportionate. The ESAs are proposing to introduce a proportionality threshold whereby a PRIIP manufacturer would be able to use a simplified approach where there is a low number of transactions or portfolio turnover;

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

- While negative implicit transaction costs are not necessarily inaccurate, the ESAs recognize that such information may not be understood by retail investors and intend to adjust the rules such that negative transaction costs can never be disclosed.

The ESAs think that the adjustments described above to the current slippage methodology should adequately resolve the challenges that have been identified since the implementation of the methodology.

At the same time, taking into account representations from industry stakeholders, the ESAs also have been assessing whether to replace the prescriptive arrival price methodology currently stipulated in the PRIIPs Delegated Regulation with a more principles or criteria-based approach. The rationale for this approach would be to avoid any risk of inappropriate results by enabling some discretion by the PRIIP manufacturer to best reflect the features of the specific trade when evaluating implicit costs, such as the size of the order, the liquidity of the instrument, the mode of negotiation and availability of market data.

The ESAs are currently of the view that such an approach is not preferred because there would be a material risk of inconsistent applications, as well as questions or uncertainty from PRIIP manufacturers as to how to apply the criteria in a practice. At this stage, the ESAs therefore see more merit in amending the arrival price methodology (see Option 1 within Section 12.7) rather than replacing it.

However, the ESAs have decided to include draft proposals for a more principles-based approach within the consultation paper - see Option 2 within Section 12.7. This is in order to receive feedback from a range of stakeholders on whether they consider that; (1) the benefits of this type of approach outweigh the drawbacks; (2) how to best draft the corresponding requirements should this approach ultimately be preferred. As well as being less prescriptive on the use of the arrival price this alternative option also provides:

- A more general derogation from a default methodology, allowing for the use of alternative approaches (e.g. based on third party data) where justified and subject to certain criteria (e.g. representativeness of data used);
- A simplified methodology for new PRIIPs.

9. Amendments arising from the end of the exemption in Article 32 of the PRIIPs Regulation

9.1 Introduction

In the February 2019 Final Report it was stated that:

> *while any decision on the expiry of the UCITS exemption will be determined by the co-legislators, it is relevant for the ESAs to prepare for the possible inclusion of UCITS within the scope of the PRIIPs Regulation, by considering further the issues discussed in Section 4.3 of the CP and the extent to which aspects of the UCITS Regulation 583/2010 would need to be reflected within the PRIIPs Delegated Regulation.*

This Section indicates which parts of the UCITS Regulation 583/2010 should be included in the PRIIPs Delegated Regulation, in order to address the specific issues related to the potential end of the exemption for UCITS funds in the PRIIPs Regulation.

9.2 Background

The UCITS Regulation 583/2010 is composed of the following chapters:

- General principles (Chapter I – Articles 1 to 3);
- Form and presentation of the KII (Chapter II – Articles 4 to 6);
- Contents of the sections of the KII (Chapter III – Articles 7 to 24);
- Particular UCITS structures (Chapter IV – Articles 25 to 37);
- Durable medium (Chapter V – Article 38).

These requirements are complemented with several Q&As published by ESMA and presented in the section II of the ESMA Q&A on the UCITS Directive[30]. These Q&As would, however, be transferred into PRIIPs Q&As at a later stage rather than incorporated in the PRIIPs Delegated Regulation.

The following parts of this section of the consultation paper consider, chapter per chapter of the UCITS Regulation 583/2010 (except Chapter V), which of these articles or parts of articles of the UCITS

[30] https://www.esma.europa.eu/sites/default/files/library/esma34-43-392_qa_ucits_directive.pdf

Regulation 583/2010, and which corresponding Q&As, could be equally relevant in the context of this revision of the PRIIPs Delegated Regulation.

The criteria used to select those articles or parts of articles of the UCITS Regulation 583/2010 that could be included are the following:

- Whether the requirements of the UCITS Regulation 583/2010 are already covered (identical or similar requirements) in the PRIIPs Regulation or Delegated Regulation (e.g. all requirements on the UCITS risk and cost indicators would not be retained in a PRIIPs context);

- Whether the requirements of the UCITS Regulation 583/2010 are relevant in the context of the amendments envisaged to the PRIIPs Delegated Regulation as part of this CP.

Finally, the ESAs have also considered whether some of the requirements of the UCITS Regulation 583/2010 that would be relevant to include in the PRIIPs Delegated Regulation would need to be extended to other PRIIPs, such as retail AIFs (funds covered by the Directive 2011/61/EU (AIFM Directive)[31]). **When reviewing this section, stakeholders are also invited to comment on this issue.**

According to the UCITS Directive (Article 78), the UCITS KII currently needs to be provided not only to retail, but also to professional investors. Given that the PRIIPs Regulation applies to products made available to retail investors, the ESAs have worked under the legal assumption that, in the absence of further changes to the UCITS Directive, should UCITS be required to provide a PRIIPs KID to retail investors the UCITS KII may still be provided to professional investors. However, this is also subject to any decision by the co-legislators on the exemption in Article 32 of the PRIIPs Regulation.

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

Please note that all the articles of the UCITS Regulation 583/2010 which are discussed in the following subsections are included in Section 12.8 of this consultation paper as amended versions of these articles that would be included in the PRIIPs amending RTS.

The Q&A that are referred to in this Section can be found on the ESMA website: (https://www.esma.europa.eu/sites/default/files/library/esma34-43-392_qa_ucits_directive.pdf)

[31] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

9.2.1 General principles (Chapter I – Articles 1 to 3 of the UCITS Regulation 583/2010)

In relation to this chapter, it is considered whether the specification on the situation in which no management company has been designated (Article 2(2) of the UCITS Regulation) should be included in the PRIIPs Delegated Regulation.

While the PRIIPs Regulation is arguably already clear that it applies to situations in which no management company has been designated, it is proposed to include this specification in the PRIIPs Delegated Regulation to avoid any legal uncertainty.

It is proposed to include these specifications as they are currently drafted in Article 1 of the PRIIPs Delegated Regulation, under a new paragraph on UCITS and relevant non-UCITS funds.

Regarding Q&As 1a to 1c, and 2a to 2c (of the abovementioned UCITS Q&As), the ESAs are of the view that these should not be included in the PRIIPs Delegated Regulation, given that requirements on similar (but different) topics already exist in the PRIIPs context.

With respect to regular saving plans, a specific issue has however emerged in one Member State. Under the UCITS framework a specific Q&A specifies the conditions under which a KII should be delivered in those cases as follows:

> *Section II Question 2a:*
>
> *Should existing investors within a UCITS be provided with a KIID in the case of additional investments?*
>
> *Answer 2a:*
>
> *Yes. Existing investors should be provided with a KIID in the case of additional investments, on the basis that the KIID is a pre-contractual document and each additional subscription is a new contract. However, where unit holders in a UCITS invest through a regular savings plan, a KIID is not required in relation to the periodic subscriptions, unless a change is made to the subscription arrangements, for example, increases or decreases in the subscription amount, which would require a new subscription form*.

According to this Q&A the UCITS KII is provided once at the beginning of the savings plan and if the customer makes changes to his subscription. If the UCITS KII is updated due to the renewed past performance sections, for example, the existing customer will not receive the updated KII. This is explicitly stated in Q&A 2c.

In contrast to the UCITS Regulation, the PRIIPs Regulation states the following:

> Article 13(4) PRIIPs Regulation:

4. Where successive transactions regarding the same PRIIP are carried out on behalf of a retail investor in accordance with instructions given by that retail investor to the person selling the PRIIP prior to the first transaction, the obligation to provide a key information document under paragraph 1 shall apply only to the first transaction, and to the first transaction after the key information document has been revised in accordance with Article 10.

Here it is explicitly stated that the revised KID should be sent to the existing customer.

The ESAs are aware of this issue and are willing to address this potential difference between the requirements of the UCITS and PRIIPs Regulations.

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

9.2.2 Form and presentation of the KII (Chapter II – Articles 4 to 6 of the UCITS Regulation 583/2010)

From this chapter, paragraphs 4, 6 and 12 of Article 4 of the UCITS Regulation 583/2010 have been identified as relevant to include in the PRIIPs Delegated Regulation (Article 4 of the UCITS Regulation 583/2010 is entitled "Title and contents of the document").

The second and third sentences of Article 4(4) of the UCITS Regulation 583/2010 are considered to provide information which is complementary to the corresponding Articles in the PRIIPs context (in particular Articles 6 and 8 of the PRIIPs Regulation and Article 1 of the PRIIPs Delegated Regulation) and should be included in the PRIIPs Delegated Regulation. It is proposed to include these specifications as they are currently drafted in Article 1 of the PRIIPs Delegated Regulation, under a new paragraph on UCITS and relevant non-UCITS funds.

However, with respect to paragraphs 6 and 12 of Article 4, these would need to be extended to other types of PRIIPs in order to ensure consistency and a level playing field.

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

Regarding Q&As 5 and 7 (of the abovementioned UCITS Q&As), ESAs are of the view that these could be included in the PRIIPs Q&A, given that there are no exact similar requirements in the PRIIPs context.

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

Regarding Q&A 7, another option could be to keep an amended version of the Q&A in the set of UCITS Q&As.

9.2.3 Contents of the sections of the KII (Chapter III – Articles 7 to 24 of the UCITS Regulation 583/2010)

From this chapter, Articles 7, 9, 15 to 19, 20 and 21 of the UCITS Regulation 583/2010 have been identified as those which could be included in the PRIIPs Delegated Regulation.

In deviation from Article 7 (1)(b), the KII shall point to the, as the case may be, missing or restricted possibility of redemption of shares/units in the case of a closed-ended AIF, an open-ended real estate AIF or a fund of hedge funds.

With respect to Article 7, paragraphs (1)(d), (1)(e) and (2) (a to d) seem to provide information which is complementary to the corresponding Articles in the PRIIPs context (in particular Article 8 of the PRIIPs Regulation and Article 2 of the PRIIPs Delegated Regulation) and should therefore be included in the PRIIPs Delegated Regulation. These specifications would be included in Article 2 of the PRIIPs Delegated Regulation, under a new paragraph on UCITS funds.

It is to be noted that Article 7(1)(d) is key in relation to the work of ESMA on closet indexing. ESMA has indeed committed significant resources to combatting the practice of closet indexing, which is prohibited by this Article. It is a priority investor protection issue. Failure to include this provision in the PRIIPs Delegated Regulation could risk closet indexing being seen as permissible under the applicable rules.

With respect to the other parts of Article 7, these might need to be extended to other types of PRIIPs in order to ensure consistency and a level playing field.

Additionally from this chapter, the following Articles seem to include information which is slightly different and complementary to the corresponding articles in the PRIIPs context:

- Article 9 (compared to Article 3 of the PRIIPs Delegated Regulation);
- Article 20 (compared in particular to Article 8 of the PRIIPs Regulation and Article 3 of the PRIIPs Delegated Regulation);
- Article 21 (compared in particular to Article 6(2) of the PRIIPs Regulation).

In the case of a closed-ended AIF and provided that investments in concrete assets have already been determined, these assets shall be described as well in addition to the minimum information according to Article 7 (1). In this case, the KII shall not exceed three pages of A4-sized paper when printed.

However these provisions may also be relevant for other types of PRIIPs and might need to be extended to other types of PRIIPs (in particular retail AIFs for Article 20), in order to ensure consistency and level playing field.

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

9.2.4 Particular UCITS structures (Chapter IV – Articles 25 to 37 of the UCITS Regulation 583/2010)

From this chapter, Articles 25 to 28, 31, 32 and 34, and Article 35 (past performance) of the UCITS Regulation 583/2010 have been identified as relevant for inclusion in the PRIIPs Delegated Regulation. These are considered provide information which is complementary to the corresponding articles in the PRIIPs context (Regulation or Delegated Regulation) and should be included in the PRIIPs Delegated Regulation, given the specificities of the particular UCITS structures which are referred to in these Articles. These specifications could be included in a new Article called "Particular UCITS structures" of the PRIIPs Delegated Regulation.

With respect to Q&A 3 on share classes (of the abovementioned UCITS Q&A), it is considered relevant to include it in the PRIIPs Q&As, alongside Article 26 of the UCITS Regulation 583/2010 on the same topic.

With respect to Article 35 on past performance of master / feeder UCITS, if it is proposed to include information on past performance in the PRIIPs KID, this provides information which is expected to be relevant in the PRIIPs context as well (in Article 3 of the PRIIPs Delegated Regulation).

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

10. PRIIPs offering a range of options for investment

10.1 Introduction

This Section presents the ESAs' draft proposals to amend the rules in Chapter II (Articles 10 to 14) of the PRIIPs Delegated Regulation, which address the rules for PRIIPs offering a range of options for investment or so-called multi-option products (MOPs). The ESAs' work on this topic follows their statement in the February 2019 Final Report that this was a priority area for this review:

> *"the information gathered by the ESAs following the implementation of the KID would indicate that, where the approach in Article 10(b) of the PRIIPs Delegated Regulation is applied (i.e. the use of a "generic KID"), there are challenges for retail investors to understand the interaction between the "generic KID" and the "specific information" for the underlying investment option, and to compare between different multi-option products (MOPs), in particular concerning the costs. While such challenges may arise from the disclosure of two types of pre-contractual information documents (the UCITS KIID and the PRIIPs KID) which can render difficult the comparability and aggregation at the level of the contract, it is considered relevant to examine more generally whether the approach in Article 10(b) is delivering an appropriate outcome for the retail investor and to assess whether regulatory changes would be necessary, or improvements can be made by providing additional guidance."*

The current PRIIPs Delegated Regulation provides for two different approaches for how to structure the KID for these types of products:

- A separate KID can be prepared for each investment option (Article 10(a));
- A generic KID covering in general terms the types of investment options offered and separate information on each underlying investment option (Article 10(b)).

Another important element of the current approach to MOPs, is that while UCITS are exempt from the PRIIPs Regulation, where a MOP manufacturer offers UCITS as investment options, they are permitted to refer the retail investor to the UCITS KII document for information on such investment options.

Draft legislative proposals to amend the current PRIIPs Delegated Regulation for MOPs are set out in Section 12.9.

10.2 The use of UCITS KII

As the ESAs noted in their November 2018 CP, several provisions in this section of the PRIIPs Delegated Regulation are directly linked to the exemption for UCITS. These provisions in Articles 12, 13 and 14 of the PRIIPs Delegated Regulation allow the use of the UCITS KII document or information drawn from the UCITS KII document to be used to comply with obligations under PRIIPs. If UCITS would prepare a PRIIPs KID from 2022 onwards, these provisions would necessarily be defunct.

As the ESAs noted in February of this year, if the UCITS KII document is no longer used to provide information on underlying investment options then such information should be provided on a comparable basis using the PRIIPs methodologies. This should better enable retail investors to compare between different MOPs and contractual options, and to aggregate the costs that they can expect to pay, i.e. both those arising from the specific investment option and the insurance contract.

10.3 Other proposals related to the use of the generic KID approach (Article 10(b) of the PRIIPs Delegated Regulation)

10.3.1 ESA analysis of current issues

The ESAs' analysis of the implementation of the rules for MOPs indicates some significant challenges regarding the clarity and usefulness of the information currently provided.

The main issues are considered to be following:

- Where a generic KID is used (in accordance with Article 10(b) of the PRIIPs Delegated Regulation) it is difficult for the investor to identify the total costs related to a particular investment option. This arises because the generic KID shows a range of costs, but does not always identify which costs are specific to an investment option and which costs relate to the insurance contract. At the same time, it is understood that the information on the underlying investment option (in accordance with Article 14 of the PRIIPs Delegated Regulation), does not usually include the total costs of investing in that option. Therefore, it is often not possible for the investor to identify from the generic KID the costs that may apply in addition to those shown in the option-specific information.

- The current rules focus on the perspective of a selection between different investment options. In practice, many MOPs allow investors to allocate their premiums between different underlying investment options at the same time, for example in order to find the assets allocation that best meets their risks and investment objectives. Information on the combination of options is not explicitly required by the PRIIPs Delegated Regulation and is often not provided within the KID documentation.

The ESAs also considered the effectiveness in general of the approach to show ranges in the generic KID. These can provide a relevant indication of how the costs and risk of the product vary depending on the investment option(s) selected. At the same time, depending on the nature of the MOP, some challenges have been identified based on the current approach. In particular, where very wide cost ranges are shown, it can be argued that the usefulness of this information is quite limited. This provides the retail investor with only a general idea of what the costs will be depending on their choices. They can only know that costs may fluctuate a lot and what the extremes of their fluctuations are.

10.3.2 New approach for the most commonly selected options

If PRIIP manufacturers were required to include in the option-specific information the total costs of investing in that option, this can be seen to provide more complete information to the investors. However, it is recognized that this would raise significant practical challenges and that it may not be proportionate to require this in all cases. Such an approach also does not address the issue related to the combination of options.

Taking this into account, the ESAs consider that a proportionate way forward, but which can bring meaningful improvements, is to introduce some differentiation between the approaches used for different types of options. More specifically, it is proposed to apply this approach as follows:

- The PRIIP manufacturer would be required to provide more complete or "total" information[32] in relation to a limited number of most relevant options or combination of options;
- For the other options, the PRIIP manufacturer would be subject to the existing approach in PRIIPs Delegated Regulation;
- The most relevant options or combination or options is defined as those (expected to be the) most frequently selected, and it is proposed to establish a link between this provision and the product oversight and governance requirements[33];
- The PRIIP manufacturer would need to apply this approach to a minimum of four options or combination of options. This minimum is considered to be necessary to enable the diversity of investment objectives or risk exposures that the MOP may offer to be reflected;
- The approach would not be required where there is minimal or only "linear" costs applied at the level of the insurance contracts, which is defined as costs that are a fixed monetary amount or only biometric risk costs.[34]

Given that this approach would apply to a limited number of options, it is not considered to be unduly burdensome and it is not expected to result in material changes to the types of products currently offered. In particular, while it focuses on a subset of options[35], it does not aim to promote a reduction in the number of options that are offered.

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

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

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[32] This means that the information would cover all of the costs and risks of investing in a particular option (or combination of options) within the MOP, as well as and potential performance from this perspective. This therefore provides a "complete" product perspective.

[33] Article 25 of Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution.

[34] These costs are already separately disclosed in the KID.

[35] Where four or more options are offered within the MOP.

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

10.3.3 Adjustments to the current approach

The ESAs also propose to introduce a number of adjustments to the existing requirements for the generic KID and option-specific information including:

- To require the PRIIP manufacturer to include a short narrative so that the retail investor is aware whether the costs shown in the specific information document include all of the costs that they will have to pay when investing in that investment option via the MOP. It is not proposed to prescribe this narrative to allow the MOP manufacturer to tailor the explanation to the particular MOP. The intention is for it to be a simple explanation highlighting whether or not all costs are shown, rather than necessarily explaining the details of those additional costs. Some possible examples are:
    - The tables below set out the costs of investing in this fund through [add product name], [where applicable for an externally managed fund] and include both our costs [i.e. the insurance company] and the costs of [external fund manager];
    - The tables below set out the costs of investing in this fund. You will have to pay additional costs which are set out in the [add appropriate cross-reference].
- To include some further specifications regarding the structure of the information to be provided on the specific investment options and the link between the generic KID and the specific information. These follow the Q&A on this issue that the ESAs published in April 2019[36].

10.3.4 Use of ranges within the generic KID

The ESAs considered if there is a relevant way to narrow the costs ranges or provide more specific information. One option to address this would be to introduce different rows per risk class in the current cost Table 1 "costs over time". This could also be relevant to show a possible link between costs and risks, and makes the diversity of choices offered as well as their consequences more visible to customers. Given that manufacturers are already expected to calculate total costs for all options in order to determine the range, this change should primarily concern the visual presentation of the KID.

[36] See ESA PRIIPs Q&A

The main drawback of this proposal is that it introduces significantly more figures in the generic KID, which may be an overload of information for certain types of retail investor.

An illustrative example of this change is provided in Section 11. It is based on a MOP that offers underlying options within all risk classes, but only multiple investment options for risk classes 2 to 6. If the MOP offered fewer risk classes, the Table would be somewhat simpler. This option is subject to the proposals made in this consultation paper to revise the Cost Tables.

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

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

11. Example KID with cost range per risk class (related to Section 10.3.4)

This example is based on the current version of the KID and does not reflect the proposed changes to the cost tables discussed in Section 8. It is included to illustrate visually the potential implications of this proposal.

What are the costs?

The overall costs of the product will depend on the investments chosen and the table below shows what the lower and higher possible costs will be for three different holding periods and for each risk class. The figures in bold characters relate to lower and higher costs taking into account all the available investments options. The figures include potential early exit penalties and assume that you invest EUR 10.000. Further details of the costs of each of the investment options available can be found in the specific information document applicable for each option. The figures are estimates and may change in the future.

Costs over Time according to the underlying options classified by risk class

Risk class to which belong the options	*Investment Eur10,000*	**If you cash in after 1 year**	**If you cash in after 4 years**	**If you cash in after 8 years (RHP)**
1	Total costs (Euros)	**299.27**	**598.81**	**1,002.22**
	Impact on return (RIY) per year	3.02%	1.52%	1.27%
2	Total costs (Euros)	**264.75 - 419.33**	**462.87 - 1,070.16**	**736.30 - 1,923.75**
	Impact on return (RIY) per year	2.68% - 4.23%	1.17% - 2.74%	0.92% - 2.49%
3	Total costs (Euros)	**304.95 - 518.56**	**502.76 - 1,151.85**	**753.05 - 1,922.77**
	Impact on return (RIY) per year	3.11% - 5.26%	1.28% - 3.01%	0.97% - 2.63%
4	Total costs (Euros)	**463.14 - 563.16**	**1,111.10 - 1,322.45**	**1,896.51 - 2,226.49**
	Impact on return (RIY) per year	4.73% - 5.76%	2.90% - 3.48%	2.59% - 3.10%
5	Total costs (Euros)	**492.04 - 1,283.68**	**1,156.57 - 1,752.91**	**1,953.13 - 2,667.46**
	Impact on return (RIY) per year	5.08% - 13.09%	3.03% - 4.70%	2.68% - 3.80%
6	Total costs (Euros)	**1,055.88 - 1,265.07**	**1,750.95 - 2,749.08**	**2,728.47 - 5,235.13**
	Impact on return (RIY) per year	10.95% - 13.11%	4.70% - 6.91%	3.90% - 6.12%
7	Total costs (Euros)	**1,528.14**	**2,905.23**	**5,616.53**
	Impact on return (RIY) per year	15.83%	7.15%	6.22%

Composition of Costs

The table below shows:

- the impact each year of the different types of costs on the investment return you might get at the end of the recommended holding period;
- the meaning of the different cost categories.

One-off costs	Entry costs	0.26% - 0.71%	The impact of the costs you pay when entering your investment.
	Exit costs	0% - 0%	The impact of the costs of exiting your investment when it matures.
Ongoing costs	Portfolio transaction costs	0% - 0.39%	The impact of the costs of us buying and selling underlying investments for the product.
	Other ongoing costs	0.66% - 5.16%	The impact of the costs that are taken each year for managing your investments.
Incidental costs	Performance fees	0% - 0%	The impact of the performance fee.
	Carried interests	0% - 0%	The impact of carried interests.

12. Draft amendments to the PRIIPs Delegated Regulation

12.1 Revised probabilistic performance scenario methodology and presentation (amendments to Article 3 and Annexes IV and V)

Paragraph 3 of Article 3 to be amended as follows:

Article 3

'What are the risks and what could I get in return?' section

…

3. PRIIP manufacturers shall include *three* ~~four~~ appropriate performance scenarios, as set out in Annex V in the section entitled 'What are the risks and what could I get in return?' of the key information document. Those *three* ~~four~~ performance scenarios shall represent ~~a stress scenario,~~ an unfavourable scenario, a moderate scenario and a favourable scenario.

Annex IV to be amended as follows:

ANNEX IV

PERFORMANCE SCENARIOS

Number of scenarios

1. The three ~~four~~ performance scenarios under this Regulation which shall show a range of possible returns, shall be the following:

   (a) a favourable scenario;

   (b) a moderate scenario;

   (c) an unfavourable scenario;

   ~~(d) a stress scenario.~~

~~2. The stress scenario shall set out significant unfavourable impacts of the product not covered in the unfavourable scenario referred to in point 1(c) of this Annex. The stress scenario shall show intermediate periods where those periods would be shown for the performance scenarios under point 1(a) to (c) of this Annex.~~

2. An additional scenario for insurance-based investment products shall be based on the moderate scenario referred to in point 1(b), where the performance is relevant in respect of the return of the investment.

3. *The minimum investment return shall also be shown. This case shall not take into account the situation where the manufacturer or party bound to make, directly or indirectly, relevant payments to the investor is not able to pay.*

Calculation of scenario values for the recommended holding period

~~4. The scenario values under different performance scenarios shall be calculated in a similar manner as the market risk measure. The scenarios values shall be calculated for the recommended holding period.~~

4. The unfavourable scenario shall be the value of the PRIIP at the 10th percentile *of the estimated distribution of outcomes over the recommended holding period less all applicable costs.*

5. The moderate scenario shall be the value of the PRIIP at the 50th percentile *of the estimated distribution of outcomes over the recommended holding period less all applicable costs.*

6. The favourable scenario shall be the value of the PRIIP value at the 90th percentile *of the estimated distribution of outcomes over the recommended holding period less all applicable costs.*

~~7. The stress scenario shall be the value of the PRIIP that results from the methodology outlined in points 10 and 11 of this Annex for Category 2 PRIIPs and in points 12 and 13 of this Annex for Category 3 PRIIPs.~~

7. For Category 2 PRIIPs *where there is a single amount invested in the PRIIP at the start of the recommended holding period, the estimated distribution of the returns over the recommended holding period are given by a Cornish-Fisher expansion of a log-normal distribution.* The expected values at the end of the recommended holding period shall be:

~~where *N* is the number of trading periods in the recommended holding period, and where the other terms are defined in point 12 of Annex II.~~

(a) The unfavourable scenario:

$$Exp[\, g\,T + \sigma \sqrt{N} * (- 1{,}28 + 0{,}107 * \mu_1 / \sqrt{N} + 0{,}0724 * \mu 2/N - 0{,}0611 * \mu 1^2/N) - 0{,}5\, \sigma^2 N]$$

(b) The moderate scenario:

$$Exp[\, g\,T - \sigma\, \mu_1 / 6\ - 0{,}5\, \sigma^2 N]$$

(c) The favourable scenario:

$$Exp[\, g\,T + \sigma \sqrt{N} * (+ 1{,}28 + 0{,}107 * \mu_1 / \sqrt{N} - 0{,}0724 * \mu 2/N + 0{,}0611 * \mu 1^2/N) - 0{,}5\, \sigma^2 N]$$

Where g is the expected annual return of the PRIIP as specified in point 12 below, T is the length of the recommended holding period in years and where the other terms are defined in point 13 of Annex II unless noted differently in point 14 of this Annex. The expected return, g, is calculated from the weighted sum of the expected returns of the different assets that compose the PRIIP.

8. For Category 2 PRIIPs where the invested amount accrues over time, the 10^{th}, 50^{th} and 90^{th} quantiles shall be read from an estimated distribution of values at the end of the recommended holding period generated using a Monte Carlo simulation. The Monte Carlo simulation shall consist of a minimum of 50,000 paths. The methodology for constructing each path is specified in points 9-10 below.

9. Each path shall be composed of the number of periods defined by the product. The value of the product at the end of the recommended holding period is calculated by sequentially adding the additional investment amount at the start of each period to the value of the product at the end of the preceding period and calculating the amount at the end of the period.

10. For each period, the expected return of the period is calculated as follows:

(a) select a random value, y, from a uniform distribution on the interval [0,1].

(b) calculate x such that the probability of obtaining a number less than x from a normal distribution with mean zero and unit standard deviation is y.

(c) the expected return for the period is given by:

$$r = Exp[\ g\ T + \sigma \sqrt{N} * (\ x + P_1(x) * \mu_1 / \sqrt{N} + P_2(x) * \mu 2/N + P_3(x) * \mu 1^2/N) - 0,5\ \sigma^2 N]$$

Where:

g, σ, μ_1 and $\mu 2$ are the expected growth, volatility, skew and excess kurtosis as defined in point 6 above
T is the length of the period in years
N is the length of the period in days
$P_1(x) = (x^2 - 1) / 6$
$P_2(x) = (x^3 – 3*x) / 24$
$P_3(x) = (5*x - 2*x^3) / 36$

(d) the value at the end of the period is the value at the start of the period multiplied by the return r.

11. For Category 3 PRIIPs, the method shall be identical to the method specified in Annex II, points 19-23 with the adjustments specified in paragraphs 12-13 below.

12. For Category 3 PRIIPs, the historical sample of the logarithm of daily returns of each asset is shifted by a constant factor. The mean of the shifted historical sample of the logarithm of daily returns of the asset is the appropriate expected return g for that asset.

13. *The expected annual return of equity assets, real estate assets, commodity assets or credit assets is the sum of a reference rate, Rf, and an asset specific risk premium.*

(a) The reference rate shall be read from the accepted market-standard interest rate curve for the currency and country of the asset derived from the prices of sovereign bonds of the country.

(b) Each asset class listed below shall have a risk premium:

(i) Equity assets: shares or indexes formed from the weighted sum of equity share prices.

- *The risk premium shall be composed of:*
  - *Dividend rate of the appropriate country/sector of the company estimated from an appropriate source if the dividend is received by the holder of the PRIIP.*
  - *Share buyback rate if shares are expected to be bought back by the issuer.*

(ii) Real estate assets: shares or index levels that reflect the value of property.

- *Dividend rate of the PRIIP estimated from an appropriate source if the dividend is received by the holder of the PRIIP.*
- *Share buyback rate if shares are expected to be bought back by the issuer.*

(iii) Commodity assets: indexes or shares that reflect the price of raw materials:

- *Implied annual yield implied by the expected forward price of the commodity if available on a liquid market less the appropriate reference rate.*

(iv) Credit assets: bonds which promise the repayment of capital and interest over a fixed time period in return for the use of capital paid.

- *Implied annual yield implied by the current price and coupon rate of the bond less the reference rate.*

14. *The volatility, σ, for all assets is defined to be the standard deviation of the natural logarithm of daily returns measured over the past 5 years. For PRIIPs which target the replication of a specific interest rate (e.g. Money-market funds), the volatility, σ, shall be the at-the-money implied volatility of 1 year European options on a similar rate.*

~~15. For Category 2 PRIIPs, the calculation of the stress scenario has the following steps:~~

~~(a) Identify a sub interval of length *w* which corresponds to the following intervals:~~

	~~1 year~~	~~> 1 year~~
~~Daily prices~~	~~21~~	~~63~~
~~Weekly prices~~	~~8~~	~~16~~
~~Monthly prices~~	~~6~~	~~12~~

~~(b) Identify for each sub interval of length w the historical lognormal returns *rt*, where *t=t0, t1, t2, …, tN*.~~

~~(c) Measure the volatility based on the formula below starting from~~ $\cancel{t_i = t_0}$ ~~rolling until~~ $\cancel{t_i = t_{N-w}}$

~~Where~~ $\cancel{M_w}$ ~~is the count of number of observations in the sub interval and~~ $\cancel{{}^{t_{i+w}}_{t_i}M_1}$ ~~is the mean of all the historical lognormal returns in the corresponding sub interval.~~

~~(d) Infer the value that corresponds to the 99th percentile for 1 year and the 90th percentile for the other holding periods. This value shall be the stressed volatility~~ $\cancel{{}^{W}\sigma_{S}}$.

~~16. For Category 2 PRIIPs, the expected values at the end of the recommended holding period for the stress scenario shall be:~~

~~where~~ $\cancel{z_\alpha}$ ~~is a proper selected value of the PRIIP at the extreme percentile that corresponds to 1% for 1 year and to 5% for the other holding periods.~~

~~17. For Category 3 PRIIPs, the following adjustments shall be made to the calculation of favourable, moderate and unfavourable performance scenarios:~~

~~(a) the expected return for each asset or assets shall be the return observed over the period as determined under point 6 of Annex II;~~

~~(b) the expected performance shall be calculated at the end of the recommended holding period, and without discounting the expected performance using the expected risk-free discount factor.~~

~~18. For Category 3 PRIIPs, the following adjustments shall be made for the calculation of the stress scenario:~~

~~(a) Infer stress volatility~~ $\cancel{{}^{W}\sigma_{S}}$ ~~based on methodology defined in point 10(a) to (c) of this Annex;~~

~~(b) Rescale historical returns~~ $\cancel{r_t}$~~, based on the formula set out below;~~

$$\cancel{r_t^{adj} = r_t * \frac{{}^{W}\sigma_{S}}{\sigma_S}}$$

~~(c) Conduct bootstrapping on~~ $\cancel{r_t^{adj}}$ ~~as described in point 22 of Annex II;~~

~~(d) Calculate the return for each contract by summing returns from selected periods and correcting these returns to ensure that the expected return measured from the simulated return's distribution is as below~~

$$\cancel{E^*[\bar{r}_{bootstrapped}] = -0.5\,{}^{W}\sigma_S^2 N}$$

~~where $E^*[\overline{r_{bootstrapped}}]$ is the new simulated mean.~~

~~19. For Category 3 PRIIPs, the stress scenario shall be the value of the PRIIP at the extreme z_α percentile as defined in point 11 of this Annex of the simulated distribution as set out in point 13 of this Annex.~~

15. For Category 4 PRIIPs, the method under point 27 of Annex II shall be used in respect of those factors that are not observed in the market, combined as necessary with the method for Category 3 PRIIPs. The relevant methods for Category 2 PRIIPs set out in points 9 to 11 of this Annex and the relevant methods for Category 3 PRIIPs set out in points 12 to 14 of this Annex shall be used for the relevant components of the PRIIP where the PRIIP combines different components. The performance scenarios shall be a weighted average of the relevant components. Product features and capital guarantees shall be taken into consideration in the performance calculations.

16. For Category 1 PRIIPs as defined in point 4(a) of Annex II, and Category 1 PRIIPs as defined in point 4(b) of Annex II that are not futures, call options and put options traded on a regulated market or on a third-country market considered to be equivalent to a regulated market in accordance with Article 28 of Regulation (EU) 600/2014, performance scenarios shall be calculated in accordance with points 12 to 14 of this Annex.

17. For Category 1 PRIIPs, that are futures, call options and put options traded on a regulated market or on a third-country market considered to be equivalent to a regulated market in accordance with Article 28 of Regulation (EU) 600/2014, performance scenarios shall be shown in the form of pay-off structure graphs. A graph shall be included to show performance for all scenarios for the different levels of the underlying value. The horizontal axis of the graph shall show the various possible prices of the underlying value and the vertical axis shall show the profit or loss at the different prices of the underlying value. For every price of the underlying value, the graph shall show the resulting profit or loss and at which price of the underlying value the profit or loss shall be zero.

18. For Category 1 PRIIPs as defined in point 4(c) of Annex II a reasonable and conservative best estimate of the expected values for the performance scenarios set out in point 1(a) to (c) of this Annex at the end of the recommended holding period shall be provided.

The scenarios selected and shown shall be consistent with and complement the other information contained in the key information document, including the overall risk profile for the PRIIP. The PRIIP manufacturer shall ensure the consistency of the scenarios with internal product governance conclusions, including amongst other things, any stress-testing undertaken by the PRIIP manufacturer for the PRIIP, and data and analysis used for the purposes of producing the other information contained with the key information document.

The scenarios shall be selected to give a balanced presentation of the possible outcomes of the product in both favourable and unfavourable conditions, but only scenarios that can be reasonably expected shall be shown. The scenarios shall not be selected so as give undue prominence to favourable outcomes at the expense of unfavourable ones.

~~*Calculation of expected values for intermediate holding periods*~~

~~19. For PRIIPs with a recommended holding period between 1 and 3 years, performance shall be shown at 2 different holding periods: at the end of the first year and at the end of the recommended holding period.~~

~~20. For PRIIPs with a recommended holding period of 3 years or more, performance shall be shown at 3 holding periods: at the end of the first year, after half the recommended holding period rounded up to the end of the nearest year, and at the end of the recommended holding period.~~

~~21. For PRIIPs with a recommended holding period of 1 year or less, no performance scenarios for intermediate holding periods shall be shown.~~

~~22. For Category 2 PRIIPs, the values to be shown for the intermediate periods shall be calculated using the formulas in point 9 to 11 of this Annex with the *N* defined to be the number of trading periods from the start date to the end of the intermediate period.~~

~~23. For Category 1 PRIIPs and Category 4 PRIIPs, the values to be shown for the intermediate periods shall be estimated by the PRIIP manufacturer in a manner consistent with the estimation at the end of the recommended holding period. To this end, the method used to estimate the value of the PRIIP at the start of each intermediate period needs to produce the same value for the entire recommended holding period, as under the method prescribed in points 16 and 15 of this Annex respectively.~~

~~24. For Category 3 PRIIPs, to produce the favourable, moderate, unfavourable and stress scenarios at an intermediate period before the end of the recommended holding period, the manufacturer shall pick three underlying simulations as referred to in points 16 to 24 of Annex II used for the calculation of the MRM and one underlying simulation as referred to in point 13 of this Annex, on the basis of underlying levels only and in such a manner that the simulated value of the PRIIPs for that intermediate period is likely to be consistent with the relevant scenario.~~

~~(a) To produce the favourable, moderate, unfavourable and stress scenarios at an intermediate period for a Category 3 PRIIP with one underlying and whose value is known to be a increasing function of its underlying level, the manufacturer shall pick three underlying simulations as referred to in points 16 to 24 of Annex II used for the calculation of the MRM and one underlying simulation as referred to in point 13 of this Annex, leading respectively to the 90th percentile level for the favourable scenario, the 50th percentile level for the moderate scenario, the 10th percentile level for the unfavourable scenario and the percentile level that corresponds to 1% for 1 year and to 5% for the other holding periods for the stress scenario.~~

~~(b) To produce the favourable, moderate, unfavourable and stress scenarios at an intermediate period for a Category 3 PRIIP with one underlying and whose value is known to be an decreasing function of its underlying level, the manufacturer shall pick three underlying simulations as referred to in points 16 to 24 of Annex II used for the calculation of the MRM and one underlying simulation as referred to in point 13 of this Annex, leading respectively to the 90 the percentile level for the unfavourable scenario, the 50th percentile level for the moderate scenario, the 10th percentile level for the favourable scenario and the percentile level that corresponds to 1% for 1 year and to 5% for the other holding periods for the stress scenario.~~

(c) ~~To produce the favourable, moderate, unfavourable and stress scenarios at an intermediate period for a Category 3 PRIIP other than those mentioned in points (a) and (b) the manufacturer shall choose underlying values consistent with the 90th, the 50th, and the 10th percentile levels and the percentile level that corresponds to 1% for 1 year and to 5% for the other holding periods of the PRIIP and use these values as the seed values for a simulation to determine the value of the PRIIP.~~

25. ~~For Category 1 PRIIPs that are futures, call options and put options traded on a regulated market or on a third-country market considered to be equivalent to a regulated market in accordance with Article 28 of Regulation (EU) 600/2014, performance scenarios for intermediate holding periods shall not be included.~~

26. ~~For favourable, moderate and unfavourable scenarios at intermediate periods, the estimate of the distribution used to read the value of the PRIIP at different percentiles shall be consistent with the observed return and volatility observed over the past 5 years of all market instruments that determine the PRIIP's value. For the stress scenario at intermediate periods, the estimate of the distribution used to read the value of the PRIIP at different percentiles shall be consistent with the simulated distribution of all market instruments that determine the PRIIP's value as set out in points 11 and 13.~~

27. ~~The unfavourable scenario shall be the estimate of the value of the PRIIP at the start of the intermediate period consistent with the 10th percentile.~~

28. ~~The moderate scenario shall be the estimate of the value of the PRIIP at the start of the intermediate period consistent with the 50th percentile.~~

29. ~~The favourable scenario shall be the estimate of the value of the PRIIP at the start of the intermediate period consistent with the 90th percentile.~~

30. ~~The stress scenario shall be the estimate of the value of the PRIIP at the start of the intermediate period consistent with the percentile level that corresponds to 1% for 1 year and to 5% for the other holding periods of the simulated distribution as set out in point 13.~~

General requirements

19. The performance of the PRIIP shall be calculated net of all applicable costs in accordance with Annex VI for the scenario and holding period being presented.

20. *Performance shall be calculated assuming an investment amount of 10.000 euros or an amount consistent with point 90 of Annex VI.*

21. *For those PRIIPs where there is no initial investment or price paid, such as forwards, future contracts, contracts for difference or swaps, performance shall be calculated assuming a notional amount of 10.000 euros or an amount consistent with point 90 of Annex VI.*

22. Performance shall be presented in monetary units *to the nearest 10 Euros or relevant currency, showing the sum of the amounts that would be received by the investor (net of costs), during the investment period including:*

(a) the payments at the end of the period, including the capital reimbursed

(b) the coupons or other amounts received during the investment period

23. <u>*For those PRIIPs where there is no initial investment or price paid such as forwards, future contracts, contracts for difference or swaps, performance in monetary units shall show the profit or loss obtained in the period.*</u>

24. Performance shall also be presented in percentage terms, as the average annual return of the investment. That figure shall be calculated considering net performance as numerator and the initial investment amount or the price paid as denominator <u>*in accordance with the following formula:*</u>

    <u>*(net performance/ initial investment)^(1/T) – 1, if T > 1. Where T is the length of the holding period in years*</u>

25. <u>*For recommended holding periods shorter than 1 year, performance in percentage terms shall reflect the projected return over that period and not in annual basis.*</u>

26. For those PRIIPs where there is no initial investment or price paid such as forwards, future contracts, <u>*contracts for difference*</u>, or swaps, the percentage shall be calculated considering the notional value of the contract and a footnote shall be added to explain that calculation. <u>*The formula for the calculation shall be:*</u>

    <u>*(Net profit or loss / Notional Value)^(1/T) -1, if T>1.*</u>

27. <u>*The footnote shall indicate that the potential return is calculated as a percentage over the notional amount.*</u>

28. For an insurance based investment product, the following shall apply in addition to the methods referred above including under point 15 when calculating the performance scenarios in respect of the investment:

    (a) future profit participation shall be taken into account;

    (b) assumptions on future profit participation shall be consistent with the assumption on the annual rates of return of the underlying assets;

    (c) assumptions on how future profits are shared between the PRIIP manufacturer and the retail investor and other assumptions on future profit sharing shall be realistic and in line with the current business practice and business strategy of the PRIIP manufacturer. Where there is sufficient evidence that the undertaking will change its practices or strategy, the assumptions on future profit sharing shall be consistent with the changed practices or strategy. For life insurers within the scope of Directive 2009/138/EC, these assumptions shall be consistent with the assumptions on future management actions used for the valuation of technical provisions in the Solvency II-balance-sheet;

    (d) where a component of the performance relates to profit participation that is payable on a discretionary basis, this component shall only be assumed in the favourable performance scenarios:

    (e) the performance scenarios shall be calculated on the basis of the investment amounts set out in point 32 of this Annex.

Regarding Annex V the different templates currently in Annex V Part 2 for single and regular investment or premium PRIIPs would need to be updated based on the approach decided upon

following the results of the consumer testing exercise and feedback to this consultation paper. At this stage only one revised template is included for a PRIP with a single investment.

ANNEX V

METHODOLOGY FOR THE PRESENTATION OF PERFORMANCE SCENARIOS

PART 1

General presentation specifications

1. The performance scenarios shall be presented in a way that is fair, accurate, clear and not misleading, and that is likely to be understood by the average retail investor.
2. ~~Where performance scenarios may be shown only at maturity or at the end of the recommended holding period, as for the PRIIPs referred to in point 21 of Annex IV, that shall be clearly explained in the narrative set out in element E in Part 2 of this Annex.~~
3. In all cases, the narrative explanations set out in element~~s A, B, C, D and~~ F in Part 2 of this Annex shall be included, except in the case of Category 1 PRIIPs referred to in point 17 of Annex IV, where the narrative explanations set in elements G to K shall be used instead.

4. Where one of the performance scenarios shows the minimum or maximum investment return, the column 'estimated chance this scenario occurs' shall no longer include the estimated chance but should instead state either 'This is the minimum you can get' or "This is the maximum you can get'.

5. Where the product is called or cancelled before the end of the recommended holding period according to the simulation, the presentation of the performance scenarios should be adjusted accordingly and explanatory notes added, in a way that it is clear whether a certain scenario includes an early call or cancellation and any reinvestment assumption that has been applied.

PART 2

Presentation of performance scenarios

For all PRIIPs except for category 1 PRIIPs referred to in point 17 of Annex IV, PRIIP manufacturers shall present the performance scenarios by means of the formats below, depending on whether the PRIIP is a single investment or premium or a regular payment or premium PRIIP. ~~The interim periods may differ depending on the length of the recommended holding period.~~ For insurance-based investment products additional rows are included in respect of the scenario for the insurance benefits including the cumulative biometric risk premium for a regular premium insurance-based investment product. Returns for that scenario shall only be shown in absolute values.

Template A: Single investment and/or single premium is paid.

Single investment paid

Performance Scenario Examples

- ***What you will get from this product depends on future market performance. Market developments in the future are uncertain and cannot be accurately predicted***
- ***The scenarios shown are only estimates of some of the possible returns that you could get based on the long-term performance of financial markets***

Example Investment amount: [EUR 10.000 / 1.000]
Recommended holding period: [x days / months / years]

Scenarios	***What you might get back after costs after [recommended holding period]***	***Average return [per year / over recommended holding period]***	***Estimated chance this scenario occurs***
Minimum	*If there is no minimum guaranteed return* ***[There is no minimum guaranteed return. You could lose some or all of your investment.]*** *If there is a minimum guaranteed return this should be stated as a figure.*		
Unfavourable	*€*	*%*	*10 in 100 chance you do worse*
Moderate	*€*	*%*	*50 in 100 chance you do worse*
Favourable	*€*	*%*	*90 in 100 chance you do worse*

Single premium paid

[To be added in Final amendments]

Template B: regular investments and/or premiums are paid.

Regular investments paid

[To be added in Final amendments]

Regular premiums paid

[To be added in Final amendments]

Performance scenarios

~~[Element A] This [table/graph] shows the money you could get back over the next [recommended holding period] years, under different scenarios, assuming that you invest EUR […] [per year].~~

~~[Element B] The scenarios shown illustrate how your investment could perform. You can compare them with the scenarios of other products.~~

~~[Element C] The scenarios presented are an estimate of future performance based on evidence from the past on how the value of this investment varies, and are not an exact indicator. What you get will vary depending on how the market performs and how long you keep the investment/product.~~

~~[Element D] The stress scenario shows what you might get back in extreme market circumstances, and it does not take into account the situation where we are not able to pay you.~~

[Where applicable][Element E] This product cannot be [easily] cashed in. This means it is difficult to estimate how much you would get back if you cash in before [the end of the recommended holding period/maturity]. You will either be unable to cash in early or you will have to pay high costs or make a large loss if you do so.

[Element F] The figures shown include all the costs of the product itself, [where applicable]:[but may not include all the costs that you pay to your advisor or distributor][and includes the costs of your advisor or distributor]. The figures do not take into account your personal tax situation, which may also affect how much you get back.

[Element G] This graph illustrates how your investment could perform. You can compare them with the pay-off graphs of other derivatives.

[Element H] The graph presented gives a range of possible outcomes and is not an exact indication of what you might get back. What you get will vary depending on how the underlying will develop. For each value of the underlying, the graph shows what the profit or loss of the product would be. The horizontal axis shows the various possible prices of the underlying value on the expiry date and the vertical axis shows the profit or loss.

[Element I] Buying this product holds that you think the underlying price will [increase/decrease].

[Element J] Your maximum loss would be that you will lose all your investment (premium paid).

[Element K] The figures shown include all the costs of the product itself, but may not include all the costs that you pay to your advisor or distributor. The figures do not take into account your personal tax situation, which may also affect how much you get back.

12.2 Use of illustrative performance scenarios instead of probabilistic scenarios (Category 3 PRIIPs) (amendments to Article 3 and new Annex VIII)

Paragraph 1 of Article 3 to be amended as follows and new paragraph 6 added:

Article 3

'What are the risks and what could I get in return?' section

1. In the section entitled 'What are the risks and what could I get in return?' of the key information document, PRIIP manufacturers shall apply the methodology for the presentation of risk as set out in Annex II, include the technical aspects for the presentation of the summary risk indicator as set out in Annex III and comply with the technical guidance, the formats and the methodology for the presentation of performance scenarios, as set out in Annexes IV and V *<u>for Category 1, 2 and 4 PRIIPs, and comply with the technical guidance and methodology for the presentation of illustrative scenarios as set out in Annex VIII for Category 3 PRIIPs</u>*.

<u>...</u>

6. *<u>For Category 3 PRIIPs, performance scenarios shall be included in the form of illustrative scenarios as set out in Annex VIII in the section entitled 'What are the risks and what could I get in return?' of the key information document.</u>*

New Annex VIII to be added:

ANNEX VIII

(New Annex based on Article 36 of UCITS Regulation 583/2010)

METHODOLOGY AND PRESENTATION OF ILLUSTRATIVE SCENARIOS

1. The illustrative scenarios shall show at least three scenarios of the PRIIP's potential performance. Appropriate scenarios shall be chosen to show the circumstances in which the formula or pay-off terms may generate a low, a medium or a high return, including, where applicable, a negative return for the investor.

2. The scenarios referred to in paragraph 1 shall enable the investor to understand fully all the effects of the calculation mechanism embedded in the formula. They shall be presented in a way that is fair, clear and not misleading, and that is likely to be understood by the average retail investor. In particular, they shall not artificially magnify the importance of the final performance of the PRIIP.

3. The scenarios referred to in paragraph 1 shall be based on reasonable and conservative assumptions about future market conditions and price movements.

4. However, whenever the formula exposes investors to the possibility of substantial losses, such as a capital guarantee that functions only under certain circumstances, these losses shall be appropriately illustrated, even if the probability of the corresponding market conditions is low.

5. The returns presented in the illustrative scenarios shall be calculated net of all applicable costs in accordance with Annex VI for the scenario and holding period presented.

6. The scenarios referred to in paragraph 1 shall be shown under the heading 'Performance scenarios – illustration of performance in specific market situations'.

7. The scenarios shall be accompanied by the following statements:

> *What you will get from this product depends on future market performance. Market developments in the future are **uncertain** and cannot be accurately predicted*
>
> *The scenarios shown are **only examples** of some of the possible returns that you could get in different scenarios that we have selected.*
>
> *The scenarios are not all equally likely to occur.*

12.3 Use of illustrative performance scenarios as well as probabilistic scenarios (Category 3 PRIIPs) (amendments to Article 3 and new Annex VIII)

Paragraph 1 of Article 3 to be amended as follows and new paragraph 6 added:

Article 3

'What are the risks and what could I get in return?' section

1. In the section entitled 'What are the risks and what could I get in return?' of the key information document, PRIIP manufacturers shall apply the methodology for the presentation of risk as set out in Annex II, include the technical aspects for the presentation of the summary risk indicator as set out in Annex III and comply with the technical guidance, the formats and the methodology for the presentation of performance scenarios, as set out in Annexes IV and V *and for Category 3 PRIIPs additionally comply with the technical guidance and methodology for the presentation of illustrative scenarios as set out in Annex VIII*.

…

6. For Category 3 PRIIPs, in addition, illustrative scenarios as set out in Annex VIII shall be included in the section entitled 'What are the risks and what could I get in return?' of the key information document to show how the formula works or how the pay-off is calculated.

New Annex VIII to be added:

ANNEX VIII

(New Annex based on Article 36 of UCITS Regulation 583/2010)

METHODOLOGY AND PRESENTATION OF ILLUSTRATIVE SCENARIOS

1. The illustrative scenarios shall show at least three scenarios of the PRIIP's potential performance. Appropriate scenarios shall be chosen to show the circumstances in which the formula or pay-off terms may generate a low, a medium or a high return, including, where applicable, a negative return for the investor.

2. The scenarios referred to in paragraph 1 shall enable the investor to understand fully all the effects of the calculation mechanism embedded in the formula. They shall be presented in a way that is fair, clear and not misleading, and that is likely to be understood by the average retail investor. In particular, they shall not artificially magnify the importance of the final performance of the PRIIP.

3. The scenarios referred to in paragraph 1 shall be based on reasonable and conservative assumptions about future market conditions and price movements.

4. However, whenever the formula exposes investors to the possibility of substantial losses, such as a capital guarantee that functions only under certain circumstances, these losses shall be appropriately illustrated, even if the probability of the corresponding market conditions is low.

5. The returns presented in the illustrative scenarios shall be calculated net of all applicable costs in accordance with Annex VI for the scenario and holding period presented.

6. The scenarios referred to in paragraph 1 shall be shown under the heading 'Table 2 – illustration of performance in specific market situations.'

7. The scenarios shall be accompanied by the following statements:

   'These are **only examples** of what you would get in different hypothetical situations.'

   The information is presented to help you understand how this product works.

   The scenarios are not all equally likely to occur.

12.4 Inclusion of information on past performance (annual) (new recital, amendments to Articles 3 and 14 and new Annexes IX and X)

New recital to be added:

Examples of situations where the benchmark index plays a role in the management of the UCITS or AIF may include the explicit or implicit definition of the portfolio's composition or the UCITS' or AIF's performance objectives and measures.

Paragraph 1 of Article 3 to be amended as follows and new paragraph 6 added:

Article 3

'What are the risks and what could I get in return?' section

1. In the section entitled 'What are the risks and what could I get in return?' of the key information document, PRIIP manufacturers shall apply the methodology for the presentation of risk as set out in Annex II, include the technical aspects for the presentation of the summary risk indicator as set out in Annex III and comply with the technical guidance, the formats and the methodology for the presentation of performance scenarios, as set out in Annexes IV and V <u>*as well as with the methodology and the format for the presentation of past performance, as set out in Annexes VIII and IX*</u>.

…

6. <u>*For linear PRIIPs that are AIFs or UCITS or unit-linked insurance-based investment products, past performance shall be included in the key information document as set out in Annexes IX and X.*</u>

Paragraph 1(c) of Article 14 to be amended as follows. Please note that the additional changes to Article 14 discussed in Section 10 are not reflected here.

Article 14

Specific information on each underlying investment option

1. In relation to the specific information referred to in Articles 11, 12 and 13, PRIIP manufacturers shall include for each underlying investment option – all of the following:

    (a) a comprehension alert, where relevant;

    (b) the investment objectives, the means for achieving them, and the intended target market in accordance with paragraphs 2 and 3 of Article 2;

(c) a summary risk indicator and narrative, and performance scenarios *and, where applicable, past performance* in accordance with Article 3;

(d) a presentation of the costs in accordance with Article 5.

New Annex IX to be added:

ANNEX IX (new)

METHODOLOGY FOR THE PRESENTATION OF PAST PERFORMANCE

Definitions

1. For the purpose of determining past performance, the following definitions shall apply:

(a) "AIF" as referred to in Article 3(6) means an AIF as defined in point (a) of Article 4(1) of Directive 2011/61/EU.

(b) "UCITS" means a UCITS as defined in Article 1(2) of Directive 2009/65/EC.

(c) Linear PRIIPs as referred to in Article 3(6) are PRIIPs that meet the requirements for Category 2 PRIIPs as set out in point 5 of Annex II, except for the requirement on the availability of historical prices.

(d) Internal funds as referred to in Article 14 (e) are internal funds provided by an insurance undertaking as defined in the second subparagraph of Article 132 (3) of Directive 2009/138/EC which are underlying investment options as referred to in Articles 11, 12 and 13. Linear internal Funds are internal funds that meet the requirements for Category 2 as set out in point 5 of Annex II with respect to the exposure to the price of underlying assets.

Past performance calculation methodology for AIFs or UCITS (based on Article 16 of the UCITS Regulation 583/2010)

2. The calculation of past performance figures shall be based on the net asset value of the AIFs or UCITS, and they shall be calculated on the basis that any distributable income of the fund has been reinvested.

Use of 'simulated' data for past performance for AIFs or UCITS (based on Article 19 of the UCITS Regulation 583/2010)

3. A simulated performance record for the period before data was available shall only be permitted in the following cases, provided that its use is fair, clear and not misleading:

(a) a new share class of an existing AIF or UCITS or investment compartment may simulate its performance by taking the performance of another class, provided the two classes do not differ materially in the extent of their participation in the assets of the AIF or the UCITS;

(b) a feeder AIF or UCITS may simulate its performance by taking the performance of its master AIF or UCITS, provided that one of the following conditions are met:

(i) the feeder's strategy and objectives do not allow it to hold assets other than units of the master and ancillary liquid assets;

(ii) the feeder's characteristics do not differ materially from those of the master.

Calculation Methodology of past performance for linear unit-linked insurance-based investment products and internal funds (new)

4. The calculation methodology of past performance as described in points 1 to 2 of this Annex shall be applied mutantis mutandis to linear unit-linked insurance-based investment products and linear internal funds.

New Annex X to be added:

ANNEX X (new)

PRESENTATION OF PAST PERFORMANCE

Presentation of past performance for AIFs and UCITS (Based on Article 15 of the UCITS Regulation 583/2010 unless otherwise indicated)

1. The information about the past performance of the AIF or the UCITS shall be presented in a bar chart covering the performance of the AIF or the UCITS for the last 10 years.

   The size of the bar chart referred to in the first subparagraph shall allow for legibility, but shall under no circumstances exceed half a page in the key information document.

2. AIFs or UCITS with performance of less than 5 complete calendar years shall use a presentation covering the last 5 years only.

3. For any years for which data is not available, the year shall be shown as blank with no annotation other than the date.

4. For AIFs or UCITS which do not yet have performance data for one complete calendar year, a statement shall be included explaining that there is insufficient data to provide a useful indication of past performance to investors.

5. The bar chart layout shall be supplemented by statements which appear prominently and which:

(a) warn about its limited value as a guide to future performance using the following statement in bold letters ***(new provision)***:

> **'Past performance is not a reliable indicator of future performance. Markets could develop very differently in the future.**
>
> **It can help you to assess how the fund has been managed in the past.'**

(b) indicate briefly which charges and fees have been included or excluded form the calculation of past performance
(c) indicate the year in which the fund, compartment or share class came into existence;
(d) indicate the currency in which past performance has been calculated.

The requirement laid down in point (b) shall not apply to UCITS or AIFs which do not have entry or exit charges.

6. A key information document shall not contain any record of past performance for any part of the current calendar year.
7. The bar chart shall be presented in the section "What are the risks and what could I get in return?" of the key information document below the summary risk indicator and the performance scenarios and its narratives. The bar chart shall be presented in the subsection with the heading "Past performance". ***(New provision)***

Use of a benchmark alongside the past performance (Based on Article 18 of UCITS Regulation 583/2010 unless otherwise indicated)

8. Where the "What is this product?" section of the key information document makes reference to a benchmark, a bar showing the performance of that benchmark shall be included in the chart alongside each bar showing past performance of the AIF or the UCITS.

9. This applies for AIFs and UCITS tracking a benchmark as well as for those managed in reference to a benchmark, which is where the benchmark index plays a role in the management of the UCITS/AIFs. ***(new provision)***
10. For AIFs or UCITS which do not have past performance data over the required five or 10 years, the benchmark shall not be shown for years in which the AIF or UCITS did not exist.
11. If the AIF or UCITS is managed against a benchmark, as referred to in paragraph 9, the narrative in point 5 of this Annex shall be supplemented as follows: "This chart can help you to assess how the fund has been managed in the past and compare it to its benchmark." ***(new provision)***

12. In order to allow for a clear understanding of the differences between past performance and performance scenarios the following narrative shall be used: “This bar chart shows the fund’s performance as the percentage loss or gain per year over the last [x] years”. ***(new provision)***

Presentation of the bar chart (Based on Annex III of the UCITS Regulation 583/2010)

13. The bar chart presenting past performance shall comply with the following criteria:

(a) the scale of the Y-axis of the bar chart shall be linear, not logarithmic;

(b) the scale shall be adapted to the span of the bars shown and shall not compress

(c) the bars so as to make fluctuations in returns harder to distinguish;

the X-axis shall be set at the level of 0 % performance;

(d) a label shall be added to each bar indicating the return in percentage that was achieved;

(e) past performance figures shall be rounded to one decimal place.

Impact and treatment of material changes (Based on Article 17 of the UCITS Regulation 583/2010)

14. Where a material change occurs to an AIF’s or UCITS’ objectives and investment policy during the period displayed in the bar chart referred to in points 1 to 7 of this Annex, the AIF´s or UCITS´ past performance prior to that material change shall continue to be shown.

15. The period prior to the material change referred to in paragraph 14 shall be indicated on the bar chart and labelled with a clear warning that the performance was achieved under circumstances that no longer apply.

Use of ‘simulated’ data for past performance (Based on Article 19 of the UCITS Regulation 583/2010)

16. In all cases where performance has been calculated in accordance with point 2 of Annex IX, there shall be prominent disclosure on the bar chart that the performance has been simulated.

17. An AIF or UCITS changing its legal status but remaining established in the same Member State shall retain its performance record only where the competent authority of the Member State reasonably assesses that the change of status would not impact the AIF´s or UCITS’ performance.

18. In the case of mergers referred to in Article 2(1)(p)(i) and (iii) of Directive 2009/65/EC, only the past performance of the receiving UCITS shall be maintained in the key information document.

19. Point 18 shall also apply to mergers of AIFs.

Presentation of past performance of feeder UCITS or AIFs (Based on Article 35 of the UCITS Regulation 583/2010)

20. The past performance presentation in the key information document of the feeder UCITS or AIF shall be specific to the feeder UCITS or AIF, and shall not reproduce the performance record of the master UCITS or AIF.

21. Paragraph 20 shall not apply:

(a) where a feeder UCITS or AIF shows the past performance of its master UCITS or AIF as a benchmark; or

(b) where the feeder was launched as a feeder UCITS or AIF at a later date than the master UCITS or AIF, and where the conditions of point 2 are Annex IX are satisfied, and where a simulated performance is shown for the years before the feeder existed, based on the past performance of the master UCITS or AIF; or

(c) where the feeder UCITS has a past performance record from before the date on which it began to operate as a feeder, its own record being retained in the bar chart for the relevant years, with the material change labelled as required by point 15.

Presentation of Past Performance of linear unit-linked insurance-based investment products

22. The presentation of past performance as described in points 1 to 16 of this Annex shall be applied mutantis mutandi to linear unit-linked insurance-based investment products. ***(new provision)***

Presentation of Past Performance of linear internal funds

23. The presentation of past performance as described in points 1 to 21 of this Annex shall be applied mutantis mutandi to linear internal funds, which are investment options according to Articles 11, 12 and 13. ***(new provision)***

12.5 Inclusion of information on past performance (average over different time periods) for PRIIPs with a recommended holding period of 10 years or more (additional provisions)

The following specific provisions would be incorporated into the new Annexes IV and X as described in Section 12.4:

Presentation of past performance for PRIIPs with a recommended holding period of 10 years or more

1. For linear PRIIPs with a recommended holding period of 10 years or more that are AIFs or UCITS or unit-linked insurance-based investment products past performance shall instead be presented as set out in points 2 to 5.

2. The information about the past performance of the PRIIP shall be presented in a bar chart covering the average performance of the PRIIP over different time periods during the last 10 years.

   These time periods shall be 1 year, 3 years, 5 years and 10 years.

3. PRIIPs with performance of less than 5 complete calendar years shall use a presentation covering 1 year, 3 years and 5 years only.

4. For PRIIPs which do not yet have performance data for a complete time period, a statement shall be included explaining that there is insufficient data to provide a useful indication of past performance to investors.

5. In order to allow for a clear understanding of the differences between past performance and performance scenarios the following narrative shall be used: “This bar chart shows the product’s performance as the average percentage loss or gain over different time periods”

12.6 Revised presentation of costs (amendments to Annexes VI and VII)

12.6.1 Amendments to Annex VI

The ESAs have not included the consequential amendments to Annex VI related to the proposed changes to the cost tables in Annex VII at this stage given that a range of different options are included in the consultation paper. These amendments will be included in the final amendments.

12.6.2 Amendments to Annex VII

Annex VII to be replaced with one of the following options (1-4)

ANNEX VII

PRESENTATION OF COSTS

Option 1 (different indicator in Table 2 for PRIPs and insurance-based investment products)

What are the costs?

- *The total costs you pay and how they affect what you might get back depend on how long you hold the product and how well the product does*
- *[Where applicable, i.e. where possible]* ***Be aware that the person selling you or advising you about this product may charge you additional costs***
- *You can use the reduction in return each year due to costs* ***to compare with other products***

When you invest [10.000 / 1.000 EUR per year] ***We have assumed the product performs as shown in the moderate performance scenario***	***If you end / exit / surrender / terminate / lapse after 1 year***	***[Only for PRIIPs with RHP 8 years or more]*** ***If you end / exit / surrender / terminate / lapse after 5 years***	***If you exit after [recommended holding period] years***
Costs over time			
Total costs (EUR)	€	€	€
Impact on return over time			
Return per year before costs	%	%	%
Return per year after costs	%	%	%
Reduction in return each year due to costs	**-%**	**- %**	**-%**

Type of cost		**Description of cost**	**Only for PRIPs** **Cost if you exit after 1 year**	**Only for IBIPs** **Reduction in return each year due to costs if you exit after [RHP]**
One-off costs	***Entry costs***	**[X% of the amount invested / premium paid] or [x% of the first Y premiums / investments]** *Where the costs are embedded in the price or premium:* **These costs are already included in the [price / premium] you pay.** *[Where distribution costs are included in entry costs]* ***This includes [monetary amount] EUR costs of distribution of your product.*** *[Where the manufacturer only knows the maximum distribution cost].* **This is the maximum you could pay. The person selling you the product will inform you of the exact charge.**	€	%
	Exit costs	**X% of the value of your investment at that time.**	€	%

		Where the costs are embedded in the price: These costs will be included in the price you get. *Where they apply only for disinvestment prior to the recommended holding period.* **These costs only apply in case of** (*explain circumstances or an example in max 100 characters***: e.g. exit before maturity/termination of the product/exit out of the (monthly/….) liquidity windows).** For details refer to section "How long should I hold it and can I take my money out early?"		*[Where there are no exit costs at the recommended holding period a percentage figure is not shown but instead the following narrative]* **Exit costs do not apply at the recommended holding period**
Ongoing costs	***Management fees and other costs***	**X% of** (value of the investment / other basis) [per year / other time period] [where applicable] (**of which % are management fees)**	€	%
	Transaction costs	**X% of (value of the investment per year)** This is an estimate of the costs of us buying	€	%

		and selling underlying investments for the product.		
Incidental costs	***[Performance fees / carried interest / other]***	***X% of*** *(…describe in max 100 characters). Where applicable [cross-reference to prospectus]* *[Only include row where applicable]*	€	%

[Where applicable]: different costs apply depending on the investment amount…[explain circumstances or use an example in maximum 100 characters]

Option 2 (Simpler cost breakdown moved to Table 1)

What are the costs?

- *The total costs you pay and how they affect what you might get back depend on how long you hold the product and how well the product does.*
- *[Where applicable, i.e. where possible]* ***Be aware that the person selling you or advising you about this product may charge you additional costs***
- *You can use the reduction in return each year due to costs* ***to compare with other products.***

When you invest [10.000 / 1.000 EUR per year] ***We have assumed the product performs as shown in the moderate performance scenario***	***If you end / exit / surrender / terminate / lapse after 1 year***	***[Only for PRIIPs with RHP 8 years or more]*** ***If you end / exit / surrender / terminate / lapse after 5 years***	***If you exit after [recommended holding period] years***
Costs over time			
Entry costs	€	€	€
Ongoing costs	€	€	€
Of which, transaction costs	€	€	€
Incidental costs [where applicable]	€	€	€
Exit costs	€	€	€
Total costs	€	€	€
Impact on return over time			
Return per year before costs	%	%	%
Return per year after costs	%	%	%
Reduction in return each year due to costs	**- %**	**- %**	**-%**

Type of cost		Description of cost
One-off costs	***Entry costs***	**[X% of the amount invested / premium paid] or [x% of the first Y premiums / investments]** *Where the costs are embedded in the price or premium:* **These costs are already included in the [price / premium] you pay.** *[Where distribution costs are included in entry costs] This includes [monetary value] EUR costs of distribution of your product. [Where the manufacturer only knows the maximum distribution cost]*. **This is the maximum you could pay. The person selling you the product will inform you of the exact charge.**
	Exit costs	**X% of the value of your investment at that time.** *Where the costs are embedded in the price:* These costs will be included in the price you get. *Where they apply only for disinvestment prior to the recommended holding period.* **These costs only apply in case of** (*explain circumstances or an example in max 100 characters*: **exit before maturity/termination of the product / exit out of the (monthly/….) liquidity windows).** For details, refer to section "How long should I hold it and can I take my money out early?"
Ongoing costs	***Management fees and other costs***	**X%** of (value of the investment / other basis) [per year / other time period] [where applicable] **(of which % are management fees)**
	Transaction costs	**X% of (value of the investment per year)** This is an estimate of the costs of us buying and selling underlying investments for the product.
Incidental costs	***[Performance fees / carried interest / other]***	***X% of*** *(…describe in max 100 characters). Where applicable [cross-reference to prospectus]* *[Only include row where applicable]*

[Where applicable]: different costs apply depending on the investment amount…[explain circumstances or use an example in maximum 100 characters]

Option 3: (Table 1 only "RIY" and more "complete" second Table)

What are the costs?

- *The total costs you pay and how they affect what you might get back depend on how long you hold the product and how well the product does*
- *[Where applicable, i.e. where possible]* ***Be aware that the person selling you or advising you about this product may charge you additional costs***
- *You can use the reduction in return each year due to costs* ***to compare with other products***

When you invest [10.000 / 1.000 EUR per year] ***We have assumed the product performs as shown in the moderate performance scenario***	***If you end / exit / surrender / terminate / lapse after 1 year***	***[Only for PRIIPs with RHP 8 years or more]*** ***If you end / exit / surrender / terminate / lapse after 5 years***	***If you exit after [recommended holding period] years***
Impact on return over time			
Return per year before costs	%	%	%
Return per year after costs	%	%	%
Reduction in return each year due to costs	**- %**	**- %**	**-%**

Type of cost		Description of cost	Costs over time		
			If you end / exit / surrender / terminate / lapse after 1 year	***[Only for PRIIPs with RHP 8 years or more] If you end / exit / surrender / terminate / lapse after 5 years***	***If you exit after [recommended holding period] years***
One-off costs	***Entry costs***	**[X% of the amount invested / premium paid] or [x% of the first Y premiums / investments]** *Where the costs are embedded in the price or premium:* **These costs are already included in the [price / premium] you pay.** *[Where distribution costs are included in entry costs]* ***This includes [monetary value] EUR costs of distribution of your product.*** *[Where the manufacturer only knows the maximum distribution cost]*. This is the maximum	€	€	€

		you could pay. **The person selling you the product will inform you of the exact charge.**			
	Exit costs	**X% of the value of your investment at that time.** *Where the costs are embedded in the price:* These costs will be included in the price you get. *Where they apply only for disinvestment prior to the recommended holding period.* **These costs only apply in case of** (*explain circumstances or an example in max 100 characters*)**: exit before maturity/termination of the product / exit out of the (monthly/….) liquidity windows).** For details, refer to section "How long should I hold it and can I take my money out early?"	€	€	€
Ongoing costs	***Management fees and other costs***	**X% of** (value of the investment / other basis) [per year /	€	€	€

		other time period] [where applicable] (of which % management fees)			
	Transaction costs	**X% of (value of the investment per year)** This is an estimate of the costs of us buying and selling underlying investments for the product.	€	€	€
Incidental costs	***[Performance fees / carried interest / other]***	***X% of*** *(…describe in max 100 characters). Where applicable [cross-reference to prospectus]* *[Only include row where applicable]*	€	€	€
Total costs			€	€	€

[Where applicable]: different costs apply depending on the investment amount…[explain circumstances or use an example in maximum 100 characters]

Option 4 (Simpler cost breakdown moved to Table 1 and no separate breakdown of costs)

What are the costs?

- *The total costs you pay and how they affect what you might get back depend on how long you hold the product and how well the product does*
- *[Where applicable, i.e. where possible]* ***Be aware that the person selling you or advising you about this product may charge you additional costs***
- *You can use the reduction in return each year due to costs* ***to compare with other products***

When you invest [10.000 / 1.000 EUR per year] ***We have assumed the product performs as shown in the moderate performance scenario***	***If you end / exit / surrender / terminate / lapse after 1 year***	***[Only for PRIIPs with RHP 8 years or more]*** ***If you end / exit / surrender / terminate / lapse after 5 years***	***If you exit after [recommended holding period] years***
Costs over time			
Entry costs	€	€	€
Ongoing costs	€	€	€
Of which, transaction costs	€	€	€
Incidental costs [where applicable]	€	€	€
Exit costs	€	€	€
Total costs	€	€	€
Impact on return over time			
Return per year before costs	%	%	%
Return per year after costs	%	%	%
Reduction in return each year due to costs	**- %**	**- %**	**-%**

[Where applicable]: different costs apply depending on the investment amount…[explain circumstances or use an example in maximum 100 characters]

12.7 Revised transaction costs methodology (amendments to Annex VI points 7 to 23)

12.7.1 Option 1 – adjustments to the current arrival price methodology

Points 7 to 23 of Annex VI to be amended as follows:

Calculation of specific types of costs of investments funds

Transaction costs

7. Transaction costs shall be calculated on an annualised basis, based on an average of the transaction costs incurred by the PRIIP over the previous three years. Where the PRIIP has been operating for less than three years, transaction costs shall be calculated using the methodology set out in point *25* ~~21~~ of this Annex.

8. The aggregate transaction costs for a PRIIP shall be calculated as the sum of the transaction costs as calculated in accordance with points *9 to 29* ~~9 to 23~~ of this Annex in the base currency of the PRIIP for all individual transactions undertaken by the PRIIP in the specified period. This sum shall be converted into a percentage by dividing by the average net assets of the PRIIP over the same period.

9. *Where implicit transaction costs are negative, a minimum of explicit transaction costs shall be disclosed.*

10. When calculating the transaction costs incurred by the PRIIP over the previous three years, actual transaction costs *shall* ~~must~~ be calculated using the methodology described in points *13 to 25* ~~12 to 18~~ of this Annex for investments in the following instruments:

    (a) transferable securities as defined by Article 2 of Commission Directive 2007/16/EC[37];

    (b) other instruments that there are frequent opportunities to dispose of, redeem, or otherwise realise at prices that are publicly available to market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer.

11. Estimates of transaction costs using the methodology described below in points *24 to 26* ~~19 to 20~~ of this Annex *shall* ~~must~~ be used for investments in other instruments or assets.

Treatment of anti-dilution mechanisms

12. Where a PRIIP has a pricing mechanism that offsets the impact of dilution from transactions in the PRIIP itself, the amount of benefit accruing to the ongoing holders of the PRIIP from anti-dilution mechanisms may be deducted from the transaction costs incurred within the PRIIP using the following methodology:

[37] Commission Directive 2007/16/EC of 19 March 2007 implementing Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions (OJ L 79, 20.3.2007, p. 11).

(c) the monetary amount of any anti-dilution levy, or other payment in connection with a transaction in the PRIIP itself, that is paid to the PRIIP may be subtracted from the total transaction costs

(d) the benefit to the PRIIP of issuing units (or otherwise enabling investment in the PRIIP) at a price other than the mid price, or of cancelling units (or otherwise enabling redemption of funds from the PRIIP) at a price other than the mid price, provided that the PRIIP itself receives the benefit, shall be calculated as follows and may be subtracted from the total transaction costs:

  (i) the difference between the price of units issued and the mid price, multiplied by the net number of units issued;

  (ii) the difference between the price of units cancelled and the mid-price, multiplied by the net number of units cancelled.

Actual transaction costs

13. *Explicit costs include costs and charges incurred by the PRIIP, and paid out of investor's financial investment in the PRIIP, in order to acquire or dispose of the underlying assets of the PRIIP, such as but not limited to commissions paid to brokers or other intermediaries, stamp duty or market taxes, contract fees and execution fees for OTC derivatives, legal advisers for real estate transactions, clearing fees and booking fees charged by the custodian for other assets, where relevant.*

14. *Explicit costs shall be calculated as the sum of costs incurred by the PRIIP over the previous three years, for all individual transactions undertaken by the PRIIP and in the base currency of the PRIIP, averaged over one year. This sum shall be converted into a percentage by dividing by the average net assets of the PRIIP over the same period.*

15. The actual transaction costs for each transaction shall be calculated on the following basis:

(e) for each purchase undertaken by the PRIIP, the price of the instrument at the time the purchase order is transmitted to another person for execution (the purchase 'arrival price') shall be subtracted from the net realised execution price of the transaction. The resulting value shall be multiplied by the number of units purchased;

(f) for each sale undertaken by the PRIIP, the net realised execution price of the transaction shall be subtracted from the price of the instrument at the time the order to sell is transmitted to another person for execution (the sale 'arrival price'). The resulting value shall be multiplied by the number of units sold.

16. The net realised execution price shall be determined as the price at which the transaction is executed, including all charges, commissions, taxes and other payments (such as anti-dilution levies) associated with the transaction, either directly or indirectly, where those payments are made from the assets of the PRIIP.

17. The arrival price shall be determined as the mid-market price of the investment at the time when the order to transact is transmitted to another person. For orders that are transacted on a day that is not the day that the order was originally transmitted to another person, the arrival price shall be determined as the opening price of the investment on the day of the transaction or, where the opening price is not available,

the previous closing price. Where a price is not available at the time when the order to transact is transmitted to another person ~~(due to the order initiated outside market opening hours or in over-the-counter markets where there is no transparency of intra-day prices for example)~~, the arrival price shall be determined as the *most recently available price or, where a recent price is not available, as the* opening price on the day of the transaction or, where the opening price is not available, the previous closing price. Where an order is executed without being transmitted to another person, the arrival price shall be determined as the mid-market price of the investment at the time when the transaction was executed.

18. Where information about the time when the order to transact is transmitted to another person is not available (or not available to a sufficient level of accuracy), or where information about the price at that time is not available, it is permissible to use as the arrival price the opening price of the investment on the day of the transaction or, where the opening price is not available, the previous closing price. ~~When calculating transaction costs using data prior to 31 December 2017, intra-day prices may be considered as not available.~~

19. Costs associated with transactions undertaken by PRIIPs and concerning financial instruments that fall within one of the categories referred to in items 4 to 10 of Section C of Annex I to Directive 2014/65/EU shall be calculated in the following way:

(g) for instruments that are standardised and where there is regular trading in the instrument itself (for example an index future on a major equity index), transaction costs shall be calculated with reference to the instrument itself. The arrival price shall be determined as the mid-price of the instrument;

(h) for linear instruments that are customised, and where there is no price transparency or regular trading in the instrument itself, transaction costs shall be calculated with reference to the underlying asset(s). The arrival price shall be calculated based on the price(s) of the underlying assets, using appropriate weightings if there is more than one underlying asset. Where the cost of transacting in the instrument is materially higher than the cost of transacting in the underlying asset, this must be reflected in the transaction cost calculation;

(i) for non-linear instruments, it is permissible to calculate the transaction costs as the difference between the price paid or received for the instruments and the fair value of the instrument, on the basis described in points 36 to 46 of this Annex.

~~20. In calculating the costs associated with foreign exchange, the arrival price must reflect a reasonable estimate of the consolidated price, and must not simply be the price available from a single counterparty or foreign exchange platform, even if an agreement exists to undertake all foreign exchange transactions with a single counterparty.~~

20. By way of derogation from points 13-19 of this Annex for transactions executed on an over-the-counter basis, the actual transaction costs shall be calculated in the following way:

(a) Where a transaction is executed after bid prices and offer prices have been obtained from more than one potential counterparty, the arrival price shall be taken to be:

(i) If the best bid price is below the best offer price, the mid-point between the best bid price and best offer price;

(ii) If the best bid price is higher than the best offer price, the best bid price in the case of a sale or the best offer price in the case of a purchase.

(b) Where a transaction is executed without both bid prices and offer prices having been obtained, the transaction cost shall be calculated by multiplying the number of units transacted by half the value of the spread between the bid price and the offer price of the instrument. The value of this spread shall be calculated on the following basis:

(i) Where available, from a composite of live market bid/offer quotes; or

(ii) Where live market quotes are not available by reference, to spreads obtained *for either previous transactions in assets bearing similar characteristics (e.g. duration, maturity, coupon, call-/ put-ability) and liquidity, using transactions previously executed by the manufacturer or data verified by an independent third-party, or from an independent third-party to value the asset.*

21. In calculating the costs associated with orders that are initially entered into an auction, the arrival price shall be calculated as the mid-price immediately prior to the auction.

22. By way of derogation from points 13-21 of this Annex, where a product undertakes fewer than [250] transactions in a three-year period, or where the total consideration for all transactions undertaken over 3 years is less than [25%] of the net asset value of the product, the manager may calculate transaction costs using the methodology described in point 20.

23. In calculating the costs associated with foreign exchange, the arrival price must reflect a reasonable estimate of the consolidated price, and must not simply be the price available from a single counterparty or foreign exchange platform, even if an agreement exists to undertake all foreign exchange transactions with a single counterparty.

Transaction costs for other assets

24. In calculating the costs associated with non-financial assets, the transaction costs shall be calculated as the aggregate of the actual costs directly associated with the transaction including all charges, commissions, taxes and other payments (such as anti-dilution levies), where those assets are made from the assets of the PRIIP.

25. When estimating transaction costs for assets other than assets as referred to in point *10* ~~9~~ of this Annex, the methodology in point *14*~~12~~ of this Annex shall be used and the arrival price shall be calculated as follows:

(a) for a sale:

(i) the arrival price shall be calculated as the previous independent valuation price of the asset, adjusted for market movements, where appropriate, using an appropriate benchmark index;

(ii) where a previous independent valuation price is not available, the transaction costs must be estimated based on the difference between the transaction price and an appraisal of the fair value of the asset prior to sale;

(b) for a purchase:

(i) the arrival price shall be calculated as the previous independent valuation price of the asset, adjusted for market movements, where appropriate, using an appropriate benchmark index, where such a price is available;

(ii) where a previous independent valuation price is not available, the transaction costs must be estimated based on the difference between the transaction price and an appraisal of the fair value of the asset prior to purchase.

26. The transaction cost estimate must not be less than the amount of actual identifiable costs, *if any,* directly associated with the transaction.

Transaction costs for new PRIIPs

27. For PRIIPs that have been operating for less than 3 years and that invest predominantly in assets as referred to in point ~~9~~ *10* of this Annex, transaction costs may be calculated either by multiplying an estimate of portfolio turnover in each asset class with the costs calculated according to the methodology referred to in point (c), or as an average of the actual transaction costs incurred during the period of operation and a standardised estimate on the following basis:

(c) for the highest multiple of six months that the PRIIP has been operating, transaction costs shall be calculated on the basis described in points ~~12 to 18~~ *14 to 23* of this Annex;

(d) for the remaining period up to three years, transaction costs shall be estimated by multiplying an estimate of portfolio turnover in each asset class according to the methodology referred to in point (c);

(e) the methodology to be used differs depending on the asset class and shall be determined as follows:

(i) For the asset classes indicated in the table below, transaction costs shall be calculated as the average of the estimated cost of transaction (based on bid-ask spreads divided by two) for the relevant asset class under normal market conditions.

To estimate the cost, one or more reference indexes shall be identified for each asset class. Then, the average bid-ask spreads of the underlying indexes shall be collected. The data collected shall refer to the closing bid-ask spread at the tenth business day of each month during the last year.

The bid-ask spreads collected shall then be divided by two to obtain the estimated cost of transaction for each point in time. The average of those values is the estimated cost of transaction in each asset class under normal market conditions.

Asset Classes	
Government bonds	Government bonds and similar instruments developed market rating AAA-A
	Government bonds and similar instruments developed market different rating below A

Government bonds emerging markets (hard and soft currency)	Government bonds emerging markets (hard and soft currency)
Investment grade corporate bonds	Investment grade corporate bonds
Other corporate bonds	High yield corporate bonds

(ii) For the asset classes indicated in the table below, transaction costs (including explicit costs and implicit costs) shall be estimated either by using comparable information or by adding estimates of explicit costs to estimates of half the bid-ask spread, using the methodology described in point (i).

Asset Classes	
Liquidity	Money market instruments (for the sake of clarity, money markets funds not included)
Shares developed markets	Large-cap shares (developed markets)
	Mid-cap shares (developed markets)
	Small-cap shares (developed markets)
Shares emerging markets	Large-cap shares (emerging markets)
	Mid-cap shares (emerging markets)
	Small-cap shares (emerging markets)
Listed derivatives	Listed derivatives

(iii) For the asset classes indicated in the table below, the transaction cost is the average of the observed cost of transaction (based on bid-ask spreads divided by two) in this asset class under normal market conditions.

When identifying the observed cost of transaction, results of a panel survey may be taken into account.

Asset Classes	
OTC	OTC Exotic options
	OTC Plain vanilla options
	OTC IRS, CDS and similar
	OTC Swaps and similar instruments (different from IRS, CDS and similar)
	OTC FX Forwards developed markets
	OTC FX Forwards emerging markets

28. Estimates of portfolio turnover for a PRIIP that has been operating for less than one year must be made on a consistent basis with the investment policy disclosed in the offering documents. Estimates of portfolio turnover for a PRIIP that has been operating for more than one year must be consistent with actual portfolio turnover.

29. For PRIIPs that have been operating for less than three years and that invest predominantly in assets other than assets as referred to in point ~~9~~ *10* of this Annex, the PRIIP manufacturer shall estimate the transaction costs on the basis of the fair value method using comparable assets.

12.7.2 Option 2 – more principles-based approach to identify reference price

Points 7 to 23 of Annex VI to be replaced by the following:

Transaction costs - General

7. The information about all costs and charges, including transaction costs incurred by the PRIIP, which are not caused by the occurrence of underlying market risk, shall be calculated and disclosed to the client. Transactions costs shall include explicit charges and where applicable implicit charges.

8. Transaction costs shall be calculated using the methodology described in points 10 to 14 of this Annex for investments in the following instruments:

(a) transferable securities as defined by Article 2 of Commission Directive 2007/16/EC (1);

(b) other instruments for which there are frequent opportunities to dispose, redeem or otherwise realise at prices that are publicly available to market participants and that are either market prices or prices made available or validated by valuation systems independent of the issuer.

9. Transaction costs shall be calculated using the methodology described in points 18 to 20 of this Annex for investments in other instruments or assets.

Transaction costs for instruments defined under point 8 a) and b)

Explicit transaction costs

10. Explicit costs include costs and charges incurred by the PRIIP, and paid out of investor's financial investment in the PRIIP, in order to acquire or dispose of the underlying assets of the PRIIP, such as but not limited to commissions paid to brokers or other intermediaries, stamp duty or market taxes, contract fees and execution fees for OTC derivatives, legal advisers for real estate transactions, clearing fees and booking fees charged by the custodian for other assets, where relevant.

11. Explicit costs shall be calculated as the sum of costs incurred by the PRIIP over the previous three years, for all individual transactions undertaken by the PRIIP and in

the base currency of the PRIIP, averaged over one year. This sum shall be converted into a percentage by dividing by the average net assets of the PRIIP over the same period.

Implicit transaction costs

12. In addition, other charges, which are not explicit costs, impact the overall performance of the PRIIP when acquiring or disposing of underlying assets. These are deemed implicit costs and shall be disclosed by the manufacturer of the PRIIP to demonstrate how transactions are executed on terms that are most favourable to the client.

13. Implicit costs shall be calculated as the sum of such individual charges incurred by the PRIIP over the previous three years for all individual transactions undertaken by the PRIIP. They shall be calculated in the base currency of the PRIIP, and averaged over one year. This average annual sum shall also be converted into a percentage by dividing by the average net assets of the PRIIP over the same three year period. Where these figures are negative, implicit costs shall be deemed to be zero such that the level of transaction costs cannot be less than the amount of explicit costs.

14. Any and all processes developed by the PRIIP manufacturer to manage, mitigate and measure implicit costs shall be fit for purpose and documented in a clear and sufficiently detailed manner. Implicit costs shall be identified by comparing the execution price recorded for a specific transaction with a suitable reference price. The identification of a suitable reference price shall be duly recorded and follow the approaches set out in points (a) and (b) in a manner that is consistent with documented internal procedures of the PRIIP manufacturer to manage, mitigate and measure implicit costs, applied consistently across transaction types.

OTC transactions

15. Where the manufacturer has obtained executable prices from multiple counterparties or where live executable prices are available, implicit transaction costs shall be measured by reference to such prices. In any such case, the number of units traded shall be multiplied by either the reference price of the instrument subtracted from the execution price for each purchase undertaken by the PRIIP or the execution price subtracted from the reference price of the instrument for each sale undertaken by the PRIIP;

16. By way of derogation from point 15, where the manufacturer is able to demonstrate that the transaction data used is statistically meaningful, sufficiently granular and proper governance and controls are in place to ensure that the data is sufficiently representative of the actual trade, implicit transaction costs shall be measured by reference to prices obtained for previous transactions in assets bearing similar characteristics (e.g. duration, maturity, coupon, call- / put-ability) and liquidity, using transactions previously executed by the manufacturer or a third party or using available indexes. This derogation shall apply in all cases where a manufacturer undertakes fewer than [250] transactions in a three-year period for an individual PRIIP, or where the total consideration for all transactions undertaken over 3 years is less than [25%] of the net asset value of the product.

For transactions negotiated on platform,

17. implicit transaction costs shall be measured by reference to the price of the instrument at the time the order is transmitted by the portfolio manager or the trader or, if justified by the manufacturer on the basis of the asset type or liquidity or availability of market data, by reference to a relevant intraday price available for the day of the transaction, or by reference to the opening or previous closing price for that security where relevant. In any such case, the number of units traded shall be multiplied by either the reference price of the instrument subtracted from the execution price for each purchase undertaken by the PRIIP or the execution price subtracted from the reference price of the instrument for each sale undertaken by the PRIIP.

18. By way of derogation, where the manufacturer is able to demonstrate that the transaction data used is statistically meaningful, sufficiently granular and proper governance and controls are in place to ensure that the data is sufficiently representative of the actual trade, implicit transaction costs shall be measured by reference to prices obtained for previous transactions in the same or similar securities presenting similar characteristics (e.g. size, industry) and liquidity, deriving from transactions executed by the manufacturer or a third party or using available indexes. This derogation shall apply in all cases where a manufacturer undertakes fewer than [250] transactions in a three-year period for an individual PRIIP, or where the total consideration for all transactions undertaken over 3 years is less than [25%] of the net asset value of the product.

Transaction costs for new PRIIPs

19. For PRIIPs that have been operating for less than 3 years, transaction costs shall be estimated according to the following:

    a. estimating the total costs incurred from the costs calculated under the method described under points 10 to 14 for a period representing the highest multiple of one year that the PRIIP has been operating, averaged over one year;

    b. for a PRIIP that has been operating for less than one year, by estimating the portfolio turnover in each asset class with the costs estimated according to the methodology referred to in points 10 to 14 a (ii) and 14 b (ii) of this Annex.

20. Estimates of portfolio turnover for a PRIIP that has been operating for less than one year must be made on a consistent basis with the investment policy disclosed in the offering documents. Estimates of portfolio turnover for a PRIIP that has been operating for more than one year must be consistent with actual portfolio turnover.

21. For PRIIPs that have been operating for less than three years and that invest predominantly in assets other than assets as referred to in point 9 of this Annex, the PRIIP manufacturer shall estimate the transaction costs on the basis of the fair value method using comparable assets.

Transaction costs for assets defined under point 9

22. When estimating transaction costs for assets other than assets as referred to in point 8 of this Annex, transaction costs shall be deemed to consist of explicit costs only and shall be calculated as the aggregate of the costs directly associated with the transaction including all charges, commissions, taxes and other payments (such as anti-dilution levies), where those assets are made from the assets of the PRIIP. Where the asset has been bought or sold at a price that is materially different from its fair value, implicit costs shall be calculated as follows : (execution price – fair value price)*number of transactions.19. For assets that are not measured at fair value, transaction costs are incremental costs determined in accordance with the product's accounting policies.

23. The transaction cost estimate must not be less than the amount of actual identifiable costs directly associated with the transaction.

Treatment of anti-dilution mechanisms

24. Where a PRIIP has a pricing mechanism that offsets the impact of dilution from transactions in the PRIIP itself, the amount of benefit accruing to the ongoing holders of the PRIIP from anti-dilution mechanisms may be deducted from overall transaction costs up to an amount equal to the implicit transaction costs incurred within the PRIIP using the following methodology:

   a. the monetary amount of any anti-dilution levy, or other payment in connection with a transaction in the PRIIP itself;

   b. the benefit to the PRIIP of issuing units (or otherwise enabling investment in the PRIIP) at a price other than the mid price, or of cancelling units (or otherwise enabling redemption of funds from the PRIIP) at a price other than the mid price, provided that the PRIIP itself receives the benefit, shall be calculated as follows:

      (i) the difference between the price of units issued and the mid- price, multiplied by the net number of units issued;

      (ii) the difference between the price of units cancelled and the mid-price, multiplied by the net number of units cancelled.

12.8 Provisions to be included in PRIIPs Delegated Regulation taken from UCITS Regulation 583/2010

This section includes proposed amendments to the PRIIPs Delegated Regulation aimed at including requirements from the UCITS Regulation 583/2010 as discussed in Section 9. It is indicated below how the amendments are intended to be integrated into the PRIIPs Delegated Regulation.

Where changes are proposed to the text of the UCITS Regulation 583/2010 these are highlighted in bold (except for changes to replace "key investor information document" with "key information document").

12.8.1 General principles (Chapter I – Articles 1 to 3 of the UCITS Regulation 583/2010)

The following paragraph to be inserted into Article 1 as a new paragraph:

> *This Regulation shall apply to any investment company which has not designated a management company authorised pursuant to Directive 2009/65/EC.* **(Taken from Article 2(2) of the UCITS Regulation 583/2010)**

12.8.2 Form and presentation of the KII (Chapter II – Articles 4 to 6 of the UCITS Regulation 583/2010)

The following paragraphs to be inserted into Article 1 as new paragraphs:

> *The identification of the UCITS or AIF, including the share class or investment compartment thereof, shall be stated prominently. In the case of an investment compartment or share class, the name of the UCITS or AIF shall follow the compartment or share class name. Where a code number identifying the UCITS or AIF, investment compartment or share class exists, it shall form part of the identification of the UCITS or AIF.* **(Taken from Article 4(4) of the UCITS Regulation 583/2010)**
>
> *In addition, in cases where the **PRIIP manufacturer** forms /part of a group of companies for legal, administrative or marketing purposes, the name of that group may be stated. Corporate branding may be included provided it does not hinder an investor in understanding the key elements of the investment or diminish his ability to compare investment products* **(Taken from Article 4(6) of the UCITS Regulation 583/2010).**
>
> *Authorisation details shall consist of the following statement:*
> *'This fund (UCITS or AIF) is authorised in [name of Member State] and regulated by [identity of competent authority]'.*

In cases where the UCITS is managed by a management company exercising rights under Article 16 of Directive 2009/65/EC, an additional statement shall be included: '[Name of management company] is authorised in [name of Member State] and regulated by [identity of competent authority]'. **(Taken from Article 4(12) of the UCITS Regulation 583/2010)**

To be inserted into ESA PRIIPs Q&A or kept in UCITS Q&A

In the section 'What is this product', PRIIPs manufacturers are allowed to signpost to a glossary. However, the use of a glossary shall not result in too numerous cross-references.
The information mentioned in Article 78(4), second sub-paragraph of the UCITS Directive, on the remuneration policy which has to be made available on a website (and the paper copy of it to be made available on request) shall not be included in the PRIIPs KID. **(Taken from Q&As 5, and 7 of the section II of ESMA Q&As on the UCITS Directive)**

12.8.3 Contents of the sections of the KII (Chapter III – Articles 7 to 24 of the UCITS Regulation 583/2010)

The following paragraphs to be inserted into Article 2 as new paragraphs:

Specific contents of the description

1. The description contained in the 'What is this product' section of the key information document shall cover those essential features of the UCITS or AIF about which an investor should be informed, even if these features do not form part of the description of objectives and investment policy in the prospectus, including:

(a) the main categories of eligible financial instruments that are the object of investment;

(b) the possibility that the investor may redeem units of UCITS or AIF on demand, qualifying that statement with an indication as to the frequency of dealing in units;

(c) whether the UCITS or AIF has a particular target in relation to any industrial, geographic or other market sectors or specific classes of assets;

(d) whether the UCITS or AIF allows for discretionary choices in regards to the particular investments that are to be made, and whether this approach includes or implies a reference to a benchmark and if so, which one;

(e) whether dividend income is distributed or reinvested.

For the purposes of point (d), where a reference to a benchmark is implied, the degree of freedom available in relation to this benchmark shall be indicated, and where the UCITS or AIF has an index-tracking objective, this shall be stated.

2. The description referred to in paragraph 1 shall include the following information, so long as it is relevant:

(a) where the UCITS or AIF invests in debt securities, an indication of whether they are issued by corporate bodies, governments or other entities, and, if applicable, any minimum rating requirements;

(b) where the UCITS is a structured fund, an explanation in simple terms of all elements necessary for a correct understanding of the pay-off and the factors that are expected to determine performance, including references, if necessary, to the details on the algorithm and its workings which appear in the prospectus;

(c) where the choice of assets is guided by specific criteria, an explanation of those criteria, such as 'growth', 'value' or 'high dividends';

(d) where specific asset management techniques are used, which may include hedging, arbitrage or leverage, an explanation in simple terms of the factors that are expected to determine the performance of the UCITS or AIF;

3. Information included under paragraphs 1 and 2 shall distinguish between the broad categories of investments as specified under paragraphs 1(a), (c) and 2(a) and the approach to these investments to be adopted by a management company as specified under paragraphs 1(d) and 2 (b), (c) and (d).

4. The 'What is this product?' section of the key information document may contain elements other than those listed in paragraph 2, including the description of the UCITS or AIF' investment strategy, where these elements are necessary to adequately describe the objectives and investment policy of the UCITS or AIF.

(Taken from Article 7 of the UCITS Regulation 583/2010)

The following paragraph to be inserted into Article 2 as a new paragraph:

Principles governing the identification, explanation and presentation of risks

The identification and explanation of risks referred to in Annex II and III shall be consistent with the internal process for identifying, measuring and monitoring risk adopted by the UCITS' management company as laid down in Directive 2010/43/EU. Where a management company manages more than one UCITS, the risks shall be identified and explained in a consistent fashion.

(Taken from Article 9 of the UCITS Regulation 2010/583)

The following paragraphs to be inserted into Article 2 as new paragraphs:

Content of 'practical information' section

1. The 'What is this product?' section of the key information document shall contain the following information relevant to investors in every Member State in which the UCITS is marketed:

(a) the name of the depositary;

(b) where and how to obtain further information about the UCITS, copies of its prospectus and its latest annual report and any subsequent half-yearly report, stating in which language(s) those documents are available, and that they may be obtained free of charge;

(c) where and how to obtain other practical information, including where to find the latest prices of units;

(d) a statement that the tax legislation of the UCITS' home Member State may have an impact on the personal tax position of the investor;

2. Where the key information document is prepared for a UCITS investment compartment, the 'What is this product' section shall include the information specified in Article 25(2) (REFERENCE TO BE UPDATED IN FINAL DRAFT) including on investors' rights to switch between compartments.

3. Where applicable, the 'What is this product?' section of the key investor document shall state the information required about available share classes in accordance with Article 26 (REFERENCE TO BE UPDATED IN FINAL DRAFT).

(Taken from Article 20 of the UCITS Regulation 583/2010)

The following paragraphs to be inserted into Article 2 as new paragraphs:

Use of cross-references to other sources of information

1. Cross-references to other sources of information, including the prospectus and annual or half-yearly reports, may be included in the key information document, provided that all information fundamental to the investors' understanding of the essential elements of the investment is included in the key information document itself.

*Cross-references shall be permitted to the website of the **PRIIP or the PRIIP manufacturer**, including a part of any such website containing the prospectus and the periodic reports.'*

'2. Cross-references referred to in paragraph 1 shall direct the investor to the specific section of the relevant source of information. Several different cross-references may be used within the key information document but they shall be kept to a minimum.

(Taken from Article 21 of the UCITS Regulation 583/2010)

12.8.4 Particular UCITS structures (Chapter IV – Articles 25 to 37 of the UCITS Regulation 583/2010)

New Articles to be inserted on Particular UCITS Structures:

Investment compartments

1. Where a UCITS or AIF consists of two or more investment compartments a separate key information document shall be produced for each individual compartment.

2. Each key information document referred to in paragraph 1 shall indicate within the 'What is this product' section the following information:

(a) that the key information document describes a compartment of a UCITS or AIF, and, if it is the case, that the prospectus and periodic reports are prepared for the entire UCITS or AIF named at the beginning of the key information document;

(b) whether or not the assets and liabilities of each compartment are segregated by law and how this might affect the investor;

(c) whether or not the investor has the right to exchange his investment in units in one compartment for units in another compartment, and if so, where to obtain information about how to exercise that right.

3. Where the management company sets a charge for the investor to exchange his investment in accordance with paragraph 2(c), and that charge differs from the standard charge for buying or selling units, that charge shall be stated separately in the 'What are the costs?' section of the key information document.

(Taken from Article 25 of the UCITS Regulation 583/2010)

Share classes

Key information document for share classes

1. Where a UCITS or AIF consists of more than one class of units or shares, the key information document shall be prepared for each class of units or shares.

2. The key information document pertinent to two or more classes of the same UCITS may be combined into a single key information document, provided that the resulting document fully complies with all requirements on length, language and presentation of the PRIIPs KID.

3. The management company may select a class to represent one or more other classes of the UCITS or AIF, provided the choice is fair, clear and not misleading to potential investors in those other classes. In such cases the 'What are the risks and what could I get in return' section of the key investor document shall contain the explanation of material risk applicable to any of the other classes being represented. A key information document based on the representative class may be provided to investors in the other classes.

4. Different classes shall not be combined into a composite representative class as referred to in paragraph 3.

5. The management company shall keep a record of which other classes are represented by the representative class referred to in paragraph 3 and the grounds justifying that choice.

(Taken from Article 26 of the UCITS Regulation 583/2010)

Practical information section

If applicable, the 'What is this product?' section of the key information document shall be supplemented by an indication of which class has been selected as representative, using the term by which it is designated in the UCITS or AIF's prospectus.

That section shall also indicate where investors can obtain information about the other classes of the UCITS or AIF that are marketed in their own Member State.

(Taken from Article 27 of the UCITS Regulation 583/2010)

Fund of funds

Objectives and investment policy section

Where the UCITS invests a substantial proportion of its assets in other UCITS or other collective investment undertakings as referred to in Article 50(1)(e) of Directive 2009/65/EC, the description of the objectives and investment policy of that UCITS in the key information document shall include a brief explanation of how the other collective undertakings are to be selected on an ongoing basis.

Additionally, in the case of a fund of hedge funds the KID shall include information about the purchase of foreign target funds that are not under supervision.

(Taken from Article 28 of the UCITS Regulation 583/2010)

Feeder UCITS

Objectives and investment policy section

1. The key information document for a feeder UCITS, as defined in Article 58 of Directive 2009/65/EC, shall contain, in the description of objectives and investment policy, information about the proportion of the feeder UCITS' assets which is invested in the master UCITS.

2. There shall also be a description of the master UCITS' objectives and investment policy, supplemented as appropriate by either of the following:

> *(i) an indication that the feeder UCITS' investment returns will be very similar to those of the master UCITS; or*
>
> *(ii) an explanation of how and why the investment returns of the feeder and master UCITS may differ.*

(Taken from Article 31 of the UCITS Regulation 583/2010)

Risk and reward profile section

1. Where the risk and reward profile of the feeder UCITS differs in any material respect from that of the master, this fact and the reason for it shall be explained in the 'What are the risks and what could I get in return?' section of the key information document.

2. Any liquidity risk and the relationship between purchase and redemption arrangements for the master and feeder UCITS shall be explained in the 'What are the risks and what could I get in return? , section of the key information document.

(Taken from Article 32 of the UCITS Regulation 583/2010)

Practical information section

1. The key information document for a feeder UCITS shall contain in the ''What is this product?' section information specific to the feeder UCITS.

2. The information referred to in paragraph 1 shall include:

(a) a statement that the master UCITS' prospectus, key information document, and periodic reports and accounts are available to investors of the feeder UCITS upon request, how they may be obtained, and in which language(s);

(b) whether the items listed in point (a) are available in paper copies only or in other durable media, and whether any fee is payable for items not subject to free delivery in accordance with Article 63(5) of Directive 2009/65/EC;

(c) where the master UCITS is established in a different Member State to the feeder UCITS, and this may affect the feeder's tax treatment, a statement to this effect.

(Taken from Article 34 of the UCITS Regulation 583/2010)

12.9 PRIIPs offering a range of options for investment (amendments to Articles 10-14)

12.9.1 Main proposals

Articles 10-14 to be amended as follows:

Article 10

PRIIPs offering a range of options for investment

Where a PRIIP offers a range of underlying investment options, and the information regarding those underlying investment options cannot be provided within a single, concise, stand-alone key information document, PRIIP manufacturers shall produce one of the following:

(a)a key information document for each underlying investment option within the PRIIP including information about the PRIIP *as a whole* in accordance with Chapter I; *each key information document shall reflect the case that the retail investor invests only in that investment option*

(b)a generic key information document describing the PRIIP in accordance with Chapter I, unless otherwise specified in Articles 11 to 14, *and including an indication of where the specific information on each underlying investment option and, as the case may be, on some common combinations of options is to be found.*

Article 11

'What is this product' section in the generic key information document

In the section entitled 'What is this product' by way of derogation from paragraphs 2 and 3 of Article 2, PRIIP manufacturers shall specify the following:

(a)a description of the types of underlying investment options, including the market segments or instrument types, as well as the main factors upon which return depends;

(b)a statement indicating that the type of investors to whom the PRIIP is intended to be marketed varies on the basis of the underlying investment option *and, as the case may be, of their combinations*;

(b)bis as the case may be, the underlying investment options or combinations of options that are subject to paragraph 2 of Article 14.

~~(c)an indication where the specific information on each underlying investment option is to be found.~~

Article 12

‘What are the risks and what could I get in return?’ section in the generic key information document

1. In the section entitled ‘What are the risks and what could I get in return?’, by way of derogation from paragraphs 2(a) and 3 of Article 3, PRIIP manufacturers shall specify the following:

(a)the range of risk classes of all underlying investment options offered within the PRIIP by using a summary risk indicator having a numerical scale from 1 to 7, as set out in Annex III,

(b)a statement indicating that the risk and return of the investment varies on the basis of the underlying investment option *and, as the case may be, of their combinations*;

(c)a brief description on how the performance of the PRIIP as a whole depends on the underlying investment options *and, as the case may be, on their combinations*;

~~(d)an indication where the specific information on each underlying investment option is to be found.~~

~~2. Where PRIIP manufacturers use the key investor information document in accordance with Article 14(2), for the purposes of specifying the risk classes referred to in point (a) of paragraph 1, they shall use the synthetic risk and reward indicator pursuant to Article 8 of Regulation (EU) No 583/2010 in relation to UCITS or non-UCITS funds as underlying investment options.~~

Article 13

‘What are the costs?’ section in the generic key information document

1. In the section entitled ‘What are the costs?’, by way of derogation from Article 5(1)(b), PRIIP manufacturers shall specify the following:

(a)the range of costs for the PRIIP in the ‘Costs over time’ and ‘Composition of costs’ tables set out in Annex VII,

(b)a statement indicating that the costs to the retail investor vary on the basis of the underlying investment option *and, as the case may be, of their combinations*;

~~(c)an indication where the specific information on each underlying investment option is to be found.~~

~~2. Notwithstanding the requirements laid down in Article 5(1)(a), and by way of derogation from points 12 to 20 of Annex VI, where PRIIP manufacturers use the key investor information document in accordance with Article 14(2), they may apply the methodology set out in point 21 of Annex VI to existing UCITS or non-UCITS funds.~~

~~3. Where PRIIP manufacturers use the key investor information document in accordance with Article 14(2) with UCITS or non-UCITS funds as the only underlying investment options, by way of derogation from Article 5, they may specify the range of charges for the PRIIP in accordance with Article 10 of Regulation (EU) No 583/2010.~~

Article 14

Specific information on each underlying investment option

1. In relation to the specific information referred to in Article *10(b) this shall be provided in a specific information document, the main purpose of which is to supplement the generic key information document.*

~~s 11, 12 and 13,~~ PRIIP manufacturers shall include for each underlying investment option — all of the following:

(a) a comprehension alert, where relevant;

(b) the investment objectives, the means for achieving them, and the intended target market in accordance with paragraphs 2 and 3 of Article 2;

(c) a summary risk indicator and narrative, and performance scenarios in accordance with Article 3;

(d) a presentation of the costs in accordance with Article 5. *A statement shall also be included indicating whether or not the costs presented include all of the costs of the PRIIP in the case that the retail investor invests only in that investment option.*

(e) a reference to the PRIIPs through which the investment option is available, an indication where the generic key information document for those PRIIPs can be found and a statement that the retail investor should read the relevant generic key information document before investing in the underlying option

The information referred to in points (a) to (d) shall follow the structure of the relevant parts of the template laid down in Annex I.

2. By way of derogation from paragraph 1, the specific information document related to, at least, four commonly selected underlying investment options or combinations of options that match with distinct retail investor's profiles shall include all of the following:

(a) a comprehension alert, where relevant;

(b) *the investment objectives, the means for achieving them, and the intended target market that are specific to that option or combination of options consistently with paragraphs 2 and 3 of Article 2;*

(c) *a summary risk indicator and narrative in accordance with Article 3 that reflects the risks of the PRIIP as a whole in the case that the retail investor invests only in that investment option or combination of options*;

(c bis) *performance scenarios in accordance with Article 3 that reflects the performance of the PRIIP as a whole in the case that the retail investor invests only in that investment option or combination of options*;

(d) *a presentation of the costs of the PRIIP as a whole in the case that the retail investor invests only in that investment option or combination of options;*

(e) *a reference to the PRIIP through which the investment option or the combination of options is available, an indication where the generic key information document for that PRIIP can be found and a statement that the retail investor should read the relevant generic key information document before investing in the underlying option or combination of options.*

The underlying investment options or combinations of options subject to this paragraph shall be determined during the product approval process of the insurance-based investment product set out in Article 25 of Directive 2016/97/EC[38]. They shall reflect the scope of retail investor's investment objectives and risk tolerance that the insurance-based investment product can meet.

Without prejudice to the potential ability of the insurance-based investment product to offer several options or combinations of options that match a particular retail investor's profile, the underlying investment options or combinations of options subject to this paragraph shall be those expected to be the most frequently selected for a given retail investor's profile. The underlying investment options or combinations of options subject to this paragraph shall be reviewed in accordance with Article 15 taking into account the way that the insurance-based investment product has actually been sold.

This paragraph is not applicable when the costs of the insurance contract are defined as a fixed amount of Euro,or other currency, and neither linked to the invested amount nor the underlying investment options selected, or when these costs are exclusively biometric.

~~2. By way of derogation from paragraph 1, PRIIP manufacturers may use the key investor information document drawn up in accordance with Articles 78 to 81 of Directive 2009/65/EC to provide specific information for the purposes of Articles 11 to 13 of this Delegated Regulation where at least one of the underlying investment option referred to in paragraph 1 is a UCITS or non-UCITS fund referred to in Article 32 of Regulation (EU) No 1286/2014.~~

[38] Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution, OJ L 26, 2.2.2016, p. 19.

12.9.2 Additional option to amend Article 13 (cost table per risk class)

In addition to the amendments in Section 12.9.1 Article 13 to be amended as follows:

Article 13

'What are the costs?' section in the generic key information document

1. In the section entitled 'What are the costs?', by way of derogation from Article 5(1)(b), PRIIP manufacturers shall specify the following:

(a) the range of costs for the PRIIP in the 'Costs over time' and 'Composition of costs' tables set out in Annex VII;

In the table 'costs over time', PRIIPs manufacturers shall display separately the range of costs for each risk class within which the PRIIP offers one or more underlying investment options. In this table, figures for the cheapest and the most expensive underlying investment options for each relevant risk class shall be shown in bold characters. The options costliness is determined by the reduction in yield due to the total costs at the recommended holding period.

(b) a statement indicating that the costs to the retail investor vary on the basis of the underlying investment option.

~~(c) an indication where the specific information on each underlying investment option is to be found.~~

~~2. Notwithstanding the requirements laid down in Article 5(1)(a), and by way of derogation from points 12 to 20 of Annex VI, where PRIIP manufacturers use the key investor information document in accordance with Article 14(2), they may apply the methodology set out in point 21 of Annex VI to existing UCITS or non-UCITS funds.~~

~~3. Where PRIIP manufacturers use the key investor information document in accordance with Article 14(2) with UCITS or non-UCITS funds as the only underlying investment options, by way of derogation from Article 5, they may specify the range of charges for the PRIIP in accordance with Article 10 of Regulation (EU) No 583/2010.~~

13. Preliminary assessment of costs and benefits

13.1.1 Introduction

According to the ESAs' Regulations, the ESAs conduct analysis of costs and benefits when drafting RTS, unless such analyses are disproportionate in relation to the scope and impact of the draft RTS concerned or in relation to the particular urgency of the matter.

The draft costs and benefits analysis are subject to public consultation. When providing feedback on the potential costs and benefits, please provide data on the scale and extent of these as far as possible.

13.1.2 Baseline

When analysing the potential costs and benefits arising from the proposed options for amending the PRIIPs Delegated Regulation, these have been compared to a baseline scenario of no regulatory intervention taking place. This baseline scenario entails:

- For PRIIPs other than UCITS and relevant non-UCITS funds referred to in Article 32 of the PRIIPs Regulation, the continued application of the PRIIPs Regulation and Delegated Regulation;

- For UCITS and relevant non-UCITS funds referred to in Article 32 of the PRIIPs Regulation, the implementation of the PRIIPs KID based on the current PRIIPs Delegated Regulation in view of the expiry of the exemption in Article 32 of the PRIIPs Regulation.

13.1.3 Approach

The draft amendments to the PRIIPs Delegated Regulation presented for consultation refer to the following provisions:

(a) Article 3 ('What are the risks and what could I get in return?' section),
(b) Articles 10-14 (Specific provisions on the KID),
(c) Article 14 (Specific information on each underlying investment option),
(d) Annex IV (Performance scenarios),
(e) Annex V (Methodology for the presentation of performance scenarios),
(f) Annex VI (Methodology for the calculation of costs),
(g) Annex VII (Presentation of costs),
(h) New Annex VIII (Methodology and presentation of illustrative scenarios)
(i) New Annex IX (Methodology for the presentation of past performance), and
(j) New annex X (Presentation of past performance)

The assessment of costs and benefits focuses on the following proposed amendments which are expected to have the most material impacts:

- The inclusion of information on past performance;
- Changes to the approach or methodology for performance scenarios;
- Revisions to the methodology to calculate transaction costs;
- Revisions to the requirements for PRIIPs offering a range of options for investment (MOPs).

The amendments proposed in relation to other aspects of the PRIIPs KID either:

- Concern revisions to the presentation of information, which are discussed in general terms in the next sub-section (13.1.4); or
- Are not considered to have a material impact compared to the baseline. In these cases, the amendments are proposed primarily for the purpose of clarification.

13.1.4 Analysis of costs and benefits

General impact of changes to the KID template

Any change to the presentation and content of the KID or the methodologies underpinning it have the potential to result in substantial compliance costs for the industry, given that these changes will require:

- The update of IT systems or tools used, in particular where amendments entail changes to the KID template or its overall structure;
- PRIIP manufacturers to review and revise the KIDs for the PRIIPs that they continue to market or which continue to remain available to retail investors.

The proposed amendments entail various changes to the KID template, including the table to present performance scenarios under the section "'What are the risks and what could I get in return?" and the tables presenting costs under the section "'What are the costs?". These changes will necessitate material one-off implementation costs for existing PRIIP manufacturers. They will also entail material one-off implementation costs for PRIIP manufacturers and persons advising or selling PRIIPs to integrate the revised KID within their distribution processes.[39]

Specific impacts of the relevant changes considered

Performance scenarios and past performance

The impacts of the following changes that were considered during the policy development have been analysed:

1. Inclusion of information on past performance (where applicable)

[39] For example, for the PRIIP manufacturer to explain the changes to persons advising or selling PRIIPs and update any guidance material that they had prepared to support such persons.

- The ESAs are considering to include past performance for linear PRIIPs (AIF, UCITS and unit linked insurance-based investment products) and for linear investment options (AIFs, UCITS, internal insurance funds) based either on the current presentation of past performance in the UCITS KIID or for longer-term PRIIPs an alternative presentation using average past performance at different time periods

2. Revision of methodology for future performance scenarios
    - At this stage the ESAs intend to change the estimator of the growth rate used to show potential future performance. Instead of using the observed historic growth of the asset, the expected growth rate for a particular asset will be the sum of a reference rate common to all assets and an asset specific risk premium

3. Use of illustrative scenarios for category 3 (non-linear) PRIIPs
    - The ESAs are considering to require PRIIP manufacturers to use illustrative scenarios to show potential future performance for non-linear PRIIPs based on the approach currently used for structured UCITS

The table on the next page summarises the preliminary analysis of the ESAs regarding the expected costs and benefits of the elements being discussed.

POLICY ELEMENT	BENEFITS	COSTS
INCLUDE INFORMATION ON PAST PERFORMANCE WITHIN THE KID	Retail investors will receive additional information that may be relevant to their decision making, including to understand how effectively the product has been managed in the past and, where relevant, how it has performed against a benchmark[40]. For non-structured UCITS, consistency with the existing approach which will be beneficial for PRIIP manufacturers (limited costs) and PRIIP advisors / sellers and retail investors who are familiar with this information being displayed for UCITS. PRIIP manufacturers that see benefit in being able to disclose information	Retail investors may unduly rely on past performance information and assume it will be replicated in the future. Retail investors may find the inclusion of past performance information together with future performance scenarios confusing. The inclusion of additional information on past performance could mean that it would be more challenging for certain PRIIP manufacturers to comply with the three page limit on the length of the KID. No additional implementation costs identified for PRIIP manufacturers currently producing a KII under the UCITS regulations, which is

[40] The consumer testing being conducted should provide evidence for whether this is the case.

POLICY ELEMENT	BENEFITS	COSTS
	about the product's past performance would now be able to include such information in the KID.	considered to be the majority of PRIIP manufacturers that will be covered by this additional requirement. For non-structured funds and for linear unit-linked insurance-based investment products that do not currently prepare a KII document there are considered to be material implementation (one-off) costs and ongoing costs to review and update this information. Where it is not a new fund, such funds should have relevant information on past performance and therefore would need to prepare systems to present it in the required format.
REVISED METHODOLOGY FOR PERFORMANCE SCENARIOS	Should result in retail investors receiving information about their potential future returns that is more likely to reflect the actual returns that they will receive. Should reduce the risk that retail investors acquire unrealistic expectations about what they could get in return. PRIIP manufacturers can benefit from retail investors not having unrealistic expectations about the potential rewards from their products (e.g. potential reduced investor complaints)1-.	There will be significant implementation costs for PRIIP manufacturers to implement this change as the revised method entails some additional complexities compared to the existing approach, as well as the need to obtain the relevant market information. For example: • PRIIP manufacturers will need to decompose the assets underlying the PRIIP by asset class, country and sector or rating (rather than only using historical prices of the PRIIP or a proxy). While PRIIP manufacturers need to manage their asset allocation over time (i.e. as part of their ongoing management of the PRIIP), they are expected to need to introduce additional procedures (e.g. assessment criteria) to apply the specific methodology. They will also need to monitor the impact of changes in their asset allocation over

POLICY ELEMENT	BENEFITS	COSTS
		time. This will be more complex for multi-asset portfolios. The information needed to determine the reference rate and risk premia requires access to a market data provider. This may be difficult for PRIIP manufacturers which are smaller in size; • This information may be difficult to source for some products e.g. those based on investments in developing economies.
USE OF ILLUSTRATIVE SCENARIOS	Retail investors may be better informed about the types of factors affecting their return. For structured UCITS, consistency with the existing approach, which will be beneficial for PRIIP manufacturers (limited costs) and PRIIP advisors / sellers and retail investors who are familiar with this information being displayed for UCITS. PRIIP manufacturers may benefit from retail investors being better informed about the potential rewards from their products (e.g. potential reduced investor complaints).	Retail investors may not understand that different scenarios have different likelihoods. There is a risk of inconsistent approaches between different PRIIP manufacturers as they have some discretion to select the appropriate scenarios. Consequently, it may be more difficult for retail investors to compare between different PRIIPs. There will be significant costs for existing PRIIP manufacturers to design and implement this approach.

Revisions in other areas

The impacts of the following changes that were considered during the policy development have also been analysed:

1. More principles-based approach for methodology for transaction costs (see Option 2 within Section 12.7).

- This includes a less prescriptive approach regarding the use of the arrival price methodology to measure implicit transaction costs, as well as a more general derogation from a default methodology, allowing for the use of alternative approaches (e.g. based on third party data) where justified and subject to certain criteria (e.g. representativeness of data used)

2. New approach to present information for MOPs:
    - In this case, the PRIIP manufacturer would be required to provide more complete or "total" information in relation to a limited number (at least four) of most relevant options or combination of investment options;
    - The most relevant options or combination or options is defined as those most expected to be the most frequently selected, and it is proposed to establish a link between provision and the product oversight and governance requirements under the Insurance Distribution Directive;

The table on the next page summarises the preliminary analysis of the ESAs regarding the expected costs and benefits of the elements being discussed.

POLICY ELEMENT	BENEFITS	COSTS
REVISED METHODOLOGY FOR TRANSACTION COSTS (OPTION 2)	Transaction costs reported can be more meaningful in the case where the existing methodology may not provide a reasonable estimate of the actual transaction costs, due to the particular features of the instrument (e.g. where it is difficult to price due to being an emerging market or high yield instrument). Where it is justified to use alternative data sources (e.g. third party data) ongoing compliance costs should be reduced.	Given that the approach provides some discretion to PRIIP manufacturers (compared to the current PRIIPs Delegated Regulation) there is a risk that (subject to supervision by NCAs) there is some inconsistency in how different PRIIP manufacturers report such costs. Where such processes do not already exist, PRIIP manufacturers will need to develop new procedures with material one-off implementation costs to identify appropriate reference prices or justify the alternative (e.g. third party) data.
NEW APPROACH TO PRESENT INFORMATION FOR MOPS	Retail investors should be better informed about the features of the product. PRIIP manufacturers can benefit from being able to present information in a form that more closely reflects the nature of the	Retail investors may not always understand why information is presented differently for some underlying options compared to others.

POLICY ELEMENT	BENEFITS	COSTS
	product (e.g. ability to combine different options).	Material one-off and ongoing implementation costs for PRIIP manufacturers including to: • Identify and monitor over time the most common investment options • Prepare additional information in relation to these most common options

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

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

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