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Directorate General Financial Stability, Financial Services and Capital Markets Union

Director General

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Mr Gabriel Bernardino
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Chairman, Joint Committee of the
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Mr Andrea Enria
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Mr Steven Maijoor
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Subject: Intention of the Commission to amend the draft Regulatory Technical Standards jointly submitted by EBA, ESMA and EIOPA under Articles 8(5), 10(2) and 13(5) of Regulation (EU) No 1286/2014

Dear Mr Bernardino, Mr Enria and Mr Maijoor,

On 6 April 2016, the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA) jointly submitted to the Commission the draft regulatory technical standards (RTS) on key information documents (KID) for packaged retail and insurance-based investment products (PRIIPs).

The Commission endorsed the draft RTS on 30 June 2016 by adopting the Commission Delegated Regulation of 30 June 2016¹ (Commission Delegated Regulation). During the

¹ Commission Delegated Regulation of 30 June 2016 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 (C(2016)3999 final).

following scrutiny period, the Council raised no objections to the Commission Delegated Regulation but the European Parliament rejected it on 14 September 2016, calling for the following modifications:

- **Multi-option PRIIPs:** the treatment of multi-option PRIIPs should be clarified, in particular in relation to the explicit exemption granted to certain collective investment undertakings under the PRIIPs Regulation;
- **4th performance scenario:** the methodology for the calculation of future performance scenarios should reflect that retail investors may also lose money in an adverse scenario concerning certain PRIIPs, or in relation to certain products that have regularly led to losses over the recommended minimum holding period;
- **Comprehension alert:** detailed guidance should be provided regarding the use of the 'comprehension alert' in order to prevent inconsistent implementation of this element of the KID across the single market.

The Commission carefully assessed the choices jointly made by the three European Supervisory Authorities to allow comparability across different PRIIPs and concluded that the draft RTS marked a significant improvement in terms of transparency of those types of financial products. The Commission considers nonetheless that, in order to address the concerns expressed by the European Parliament, the following amendments to the Commission Delegated Regulation should be envisaged.

Multi-option PRIIPs

To take account of the specific nature of multi-option PRIIPs offering, as underlying investment, a range of undertakings for collective investments in transferable securities (UCITS) and other non-UCITS funds that are marketed to retail investors under national law, the Commission proposes to allow manufacturers of such multi-option PRIIPs to use the UCITS information document as an appropriate means of providing retail investors with more detailed pre-contractual information.

The proposed amendment should apply in accordance with the transitional period in the PRIIPs Regulation for UCITS and non-UCITS funds.

Fourth performance scenario

The Commission proposes the following amendments to clarify the conditions that trigger the inclusion of a fourth performance scenario in Annex IV to the Commission Delegated Regulation, and to make some consequential adjustments to the existing performance scenarios:

- to reflect a more prudent approach, the mean of historical returns should be replaced with zero. The objective is to avoid that assumptions are made on the direction of the future market expectation over the holding period in the neutral scenario;
- an additional scenario should be included — a fourth scenario that may be renamed as 'stress scenario'— showing how the PRIIP performs under stressed market conditions. The stress scenario should be mandatory as it is meant to complement the three 'normal' scenarios giving information on the possible outcome of the PRIIP where extreme market conditions materialise, given the assumptions made.

The stress scenario should be identified through a stress-test analysis of the historical volatility over a pre-defined short-term period. Taking into account possible recommended holding periods of the PRIIP and the frequency of price calculation, the following parameters should be determined:

- the length of the windows of historical returns to be considered to generate the distribution of volatility,
- the percentile of the distribution of volatility that identifies the stressed volatility,
- the percentile of the distribution of returns that identifies the stress scenario.

Comprehension alert

The Commission proposes to provide criteria in the Commission Delegated Regulation to facilitate a consistent use of the comprehension alert in the KID. Based on Recital 18 of the PRIIPs Regulation, the criteria should be the following:

- the PRIIP invests in underlying assets that are not commonly invested in by retail investors;
- the PRIIP uses a number of different mechanisms to calculate the final return of the investment, creating a greater risk of misunderstanding on the part of the retail investor;
- the investment's pay-off takes advantage of retail investor's behavioural biases, such as a teaser rate followed by a much higher floating conditional rate, or an iterative formula.

Outcomes of the PRIIPs consumer testing, as undertaken by the Commission, suggest that simple disclosure approaches are associated with better comprehension of the KID. The presentation of administrative costs in relation to biometric components of insurance-based investment products in the KID does not currently serve this purpose. The Commission therefore proposes to reduce this complexity ensuring at the same time the same level of retail investor protection through the following amendments:

- in "*What are the cost*" section, to amend the presentation of "*Ongoing costs*" by deleting "*Insurance costs*" and bundling them into the "*Other ongoing costs*"; and
- in "*What is this product*" section, to locate all the information on insurance benefits and costs.

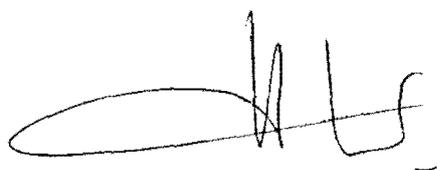
Under this approach retail investors continue to be able to identify what is invested and what relates to insurance and continue to be provided with the total cost of the PRIIPs as such as well as with insurance costs.

In light of the above considerations, and in order to ensure the required coordination with the three European Supervisory Authorities, I would like to inform you that, in accordance with the fifth and sixth subparagraphs of Article 10(1) of Regulation (EU) No 1093/2010, of Regulation (EU) No 1094/2010 and of Regulation (EU) No 1095/2010, the Commission intends to amend the draft RTS jointly submitted by EBA, EIOPA and ESMA in the way explained above and further detailed in the Annex to this letter.

I draw your attention to the sixth subparagraph of Article 10(1) of Regulation (EU) No 1093/2010, of Regulation (EU) No 1094/2010 and of Regulation (EU) No 1095/2010. According to that provision, the Authorities may amend the draft RTS within six weeks on the basis of the Commission's proposed amendments and resubmit it in the form of a formal opinion to the Commission. Due to the time constraints linked to the entry into application of the PRIIPs Regulation, I invite to submit amended RTS at your earliest convenience, and in any event within the six weeks.

The Commission would also like to invite the ESAs to develop guidance in line with the relevant provisions of the RTS and without altering their substance on the practical application of credit risk mitigation factors under the RTS for insurers.

Yours sincerely,

A handwritten signature in black ink, consisting of a large, sweeping initial 'O' followed by several vertical strokes and a final flourish.

Olivier GUERSENT

Annex: 1