

## **Comment**

**of the German Insurance Association (GDV)\***

**ID-Number 6437280268-55**

**on PRIIPs Key Information Documents**

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\*) The Berlin-based German Insurance Association (GDV) is the federation of private insurers in Germany. Its about 460 member companies offer comprehensive coverage and retirement provisions to private house-holds, trade, industry and public institutions, through 427 million insurance contracts. The German insurance industry stands for risk cover, security and financial precautions in all areas of private and public life. It makes risks calculable and bearable for individuals and it is an indispensable basis for economic activity. The insurance industry moreover provides gainful employment for 533,000 persons either as employees with insurers and in the intermediation business or as self-employed insurance intermediaries and advisers.

## Introduction

The German Insurance Association (GDV) welcomes the opportunity to respond to the ESAs' Consultation Paper on PRIIPs. We support the objective of the PRIIPs Regulation to enhance consumer protection and improve retail investor confidence in PRIIPs. Moreover, we do agree that improving the transparency of the products offered to retail investors will contribute to this aim.

However, the GDV is very concerned about the extremely short period provided for the industry to implement the key information document (KID) for PRIIPs.

On the one hand, according to the timetable pursuant the Regulation and taking into account the expected date for the Commission's adoption of the draft regulatory technical standards (RTS), as well as the European Parliament's and the Council's period for objection, there will only be 4 months for the industry to implement the KID. Such a short implementation timeframe for such a sophisticated project is unrealistic. Manufacturers will definitely need more time (at least 9 to 12 months) to develop and implement methods which will result in trustworthy, meaningful, comparable, and stable information for consumers.

However, the final stage of implementing technical specifications, programming, testing and launching by the industry can only begin once there is absolute certainty over the final presentation and content of the KID. The presentation of risk, performance and costs has been, and still is, the object of no less than three consultations. Different demanding methodologies were proposed by the European Supervisory Authorities (ESAs) and still remain to be finalised.

On the other hand, some methodologies introduced in the draft RTS – in particular on the risk indicator – are in our view unworkable, incomprehensible, incomparable, and could even lead to misleading information for consumers. Furthermore, in some cases the proposals previously suggested in the Technical Discussion Paper (TDP) were more suitable than those introduced in the RTS. The German insurers truly believe that the current draft RTS need substantial revision and improvement in order to provide consumers with meaningful information and ensure proper comparison of different products. This obviously needs more time too.

Therefore, it has now become apparent that the time needed for the appropriate development of the KID by the ESAs and implementation through the industry has been underestimated. The GDV, therefore, calls for a one-year extension of the PRIIPs implementation deadline in order to give the ESAs enough time to develop better methodology for the customers and to allow the industry to effectively implement the KID.

Furthermore, the GDV would like to highlight its key messages regarding the RTS that are reflected throughout the paper.

### **Risk**

- Forward-looking methodology previously suggested in the TDP was a good starting point for the development of a reliable risk indicator that enables a fair comparison of all PRIIPs. It is unclear why the ESAs after having already consulted four different methodologies for the risk indicator now suggest completely new methods.
- The same methodology should apply to all PRIIPs to ensure consistency and comparability, which is one of the main aims of the PRIIPs Regulation. Moreover, manufacturers will have to implement several burdensome methods for different products.
- The bootstrap methodology has severe drawbacks (e.g. it is backward-looking) and should not be used for insurance-based investment products. Cornish-Fisher method is also not suitable for products with guarantees.
- Both methodologies suggested cannot differentiate sufficiently well between different products, e.g. between different guarantee mechanisms.
- Expected Loss for a given Value-at-Risk should be used as a risk measure instead of the VaR.
- Insurance guarantee schemes and the precedence of policyholders over other claims should be taken into account as risk-mitigating factors resulting in CR1 when assessing the credit risk of insurers.
- The methods for the risk indicator should be evaluated carefully for different real-world products in order for them to be used by the industry.

### **Costs**

- The total biometric risk premium should be included in the section "What is this product?" We highly appreciate that the ESAs do not see the biometric risk premium as a cost.

- We welcome the decision to apply the Reduction in Yield (RIY) approach when determining the costs of a product.
- The information overload and complexity of costs representation should be reduced in order to enhance comprehensibility and enable comparability. Short and meaningful presentation of costs should be envisaged.
- The presentation of intermediate values in the costs section is misleading for consumers and should be avoided.
- To ensure both, comparability and a level playing field between manufacturers, only a visually highlighted RIY indicator together with annualised costs in monetary terms should be presented. Only these two figures enable comparability of products with different terms in a meaningful way.

#### **Performance scenarios**

- Performance scenarios should be prescribed. Otherwise comparability between different products cannot be ensured.
- Additional guidelines mean less time to implement meaningful, comparable and stable methods for different types of PRIIPs.

#### **Length of the document**

- The prescribed length of three pages does not seem to be realistic for some products. First, for some real-world products the KID will include more disclaimers than in those KIDs investigated in the consumer testing. Second, some products are more sophisticated than the ones that were considered.
- Translation into German could extend the text by approximately one additional page.
- It is important that the translated KIDs are also consulted with stakeholders in order to ensure that the translated terms used are meaningful and understandable for consumers.

#### **Multi-investment options PRIIPs**

- A level playing field should be ensured between different types of PRIIPs. We would like to stress that the generic KID as introduced in Article 12(1)(b) only contains high level information which is not sufficient for consumers to make an informed choice and compare different products. Therefore, the focus should be on concrete information about underlying investment options so that consumers focus on comparable information in terms of quality.

- We understand that some multi-investment options PRIIPs have many underlying investment options and it may be difficult to provide an individual KID for every single option. A solution to ensure high-quality information and a level playing field might be to divide the investment options into appropriate classes of comparable products. Then, from each class a representative KID should be chosen.

### **Delivery and review of the KID**

It should be clarified that in applying the good time requirement, the wishes of the retail investor are to be taken into account. Whether or not the purchase of a PRIIP is urgent does not only depend on purely economic considerations – e. g. where the price of the product depends on the timing – but also on the amount of time which the individual investor is willing to spend on the selection of the PRIIP. The retail investor, who, despite the explicit opportunity to take more time to reflect upon the content of the KID, chooses to proceed with the conclusion of the contract without delay, should not be artificially prevented from doing so.

Furthermore, we believe that existing mechanisms to protect the customer from the consequences of the premature conclusion of a contract should be taken into account when applying the good time requirement. In the case of insurance-based investment products, Article 186 of the Solvency II Directive stipulates a mandatory cancellation right of 14 to 30 days that does not have any economic consequences for consumers. In the case of these products, the customer is not irrevocably bound by the contract before the cancellation period has expired. Just as the good time requirement, the unilateral cancellation right serves to provide the customer with additional time to reflect on the product and to reconsider its value. Applying the good time requirement without regard to this important instrument would not be appropriate.

The proposed regulation on the review and revision of the KID for products which are not currently available to retail investors needs to be clarified since the provisions in Article 20 would still be disproportionate. The RTS should make clear that the continued obligation to review and revise the PRIIP for secondary market only targets trading by the manufacturer of the PRIIP. In the case of insurance-based investment products, manufacturers have no means to prevent individual customers from selling their product to another buyer. Thus, if the possibility of any secondary market trading without involvement of the manufacturer of the PRIIP were sufficient to trigger the obligation to review and revise, Art. 20 would in practice

never be applicable. The RTS should therefore clarify that the obligations under Articles 16 to 19 shall not apply during those periods where the PRIIP is not made available to retail investors by the manufacturer.

### **Question 1**

**Would you see merit in the ESAs clarifying further the criteria set out in Recital 18 mentioned above by way of guidelines?**

Although the criteria set out in recital 18 are unclear, there is no empowerment for the ESAs in the PRIIPs Regulation to specify the details of these criteria. If applied too broadly, the warning may lose its differentiating impact.

### **Question 2**

- (i) Would you agree with the assumptions used for the proposed default amounts? Are you of the opinion that these prescribed amounts should be amended? If yes, how and why?**
- (ii) Would you favour an approach in which the prescribed standardised amount is the default option, unless the PRIIP has a known required investment amount and price which can be used instead?**

#### Both single and regular premiums should be considered

For reasons of comparability, the GDV supports prescribed standardised amounts. However, it is also of utmost importance that both single and regular premiums are considered, as both cases are relevant in practice. The amount should be equal to the average amount invested. For insurance-based investment products a monthly on-going premium of €100 or an annual on-going premium of €1.200 (divisible by 12) could be reasonable numbers. For single premium contracts the invested amount could be €20.000. These are prudent values which should be seen as a lower limit: Due to the role of fixed costs the amounts should not be too small.

#### Terms of the products should be realistic

However, it is more important that the term of a product used in the KID is realistic. A term of 10 years was suggested for insurance-based investment products in the consumer testing. This term is unrealistically short, since many of the products have average terms of 30 years and longer.

### Question 3

**For PRIIPs that fall into category II and for which the Cornish Fisher expansion is used as a methodology to compute the VaR equivalent Volatility do you think a bootstrapping approach should be used instead? Please explain the reasons for your opinion?**

We wonder why the ESAs now suggest completely new methods for the calculation of risk without a thorough consultation of stakeholders similar to the previous consultations for the four other risk indicators. Moreover, some of the methodologies introduced in the technical discussion paper, such as a forward-looking model for the computation of the risk indicator (option 3)<sup>1</sup>, were more meaningful for long-term PRIIPs and are now completely dismissed. A proper comparability of different products and a stability of risk indicator are of utmost importance for consumers. Therefore, any newly introduced risk indicator should be thoroughly investigated by the insurance undertakings and the ESAs and it should be tested quantitatively on different real products. However, the tight schedule of this consultation does not provide stakeholders with sufficient time to detect all issues we might face when applying the indicator to products.

#### Same methodology should be applied to all products

In our view, it is essential that the same methodology is applied to all products. One of the main aims of the PRIIPs Regulation, namely to ensure comparability of different products, will not be achieved if different methods are used for different categories of PRIIPs.

In the following, we demonstrate through concrete examples that current approaches yield different methodologies for very similar products: As the Cornish-Fisher method builds on a transformation of a normal distributed random variable, it will be the better (worse) the more (less) the “true” probability distribution exhibits similarity to this transformed normal distribution. If the true underlying probability distribution is far from being (a transformed) normal – e.g. when a guarantee product is considered – this approach will yield a (potentially very) different result as compared to sampling different returns by means of Monte-Carlo simulation (e.g. applying a bootstrap methodology).

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<sup>1</sup> JC DP 2015 01, page 39

*Example 1:*

*We consider:*

- *PRIIP A: Direct investment in an investment vehicle qualifying for Category II, for which the Cornish-Fisher method shall be applied,*
- *PRIIP B: Direct investment in PRIIP A with an additional (far out of the money) guarantee of e.g. 50%. This product will fall in Category III and bootstrap methodology is applied.*

*Although both PRIIPs exhibit very similar risk exposure, the risk will be measured following two completely different methodologies which will yield different results on the risk of the products. Therefore, the GDV strongly recommends applying the same methodology for the risk indicator for all PRIIPs.*

#### Bootstrap methodology is not suitable for long-term products

We welcome that the ESAs consider stochastic models, at least for the products of Categories III and IV. In our view, this is a good starting point. Unfortunately, the bootstrap methodology has several severe drawbacks and should not be used:

1. It is backward-looking and, therefore, neither reliable nor sufficiently robust for long-term investment products: due to diversification effects of insurers' assets, five years is not a sufficiently long period to judge the performance of an insurance product. Therefore, the risk indicator will yield a distorted image if the last five years are not typical for the product. More importantly, one can artificially construct products based on assets that performed extraordinary well during the last five years compared to long-term average. These products will suggest low risk which is not true in the long term.
2. It leaves too many factors up to manufacturers' discretion such as the choice of a benchmark if the value is not observed in the market, modelling of the cover funds or surplus, which may lead to ambiguity of results.
3. It uses resampling of the daily past performance during the last five years. It is not clear how this method will apply to long-term insurance-based investment products. An insurance product typically has no "daily performance", since they are not traded on the market. And, more fundamentally, for an insurance product with a fixed term and a long duration, a five-year historical path is only (part of) one historical time series, not several realisations of a one-dimensional random variable.

### The Cornish-Fischer method is not suitable for products with guarantees

We would also like to stress that the Cornish-Fisher method is not suitable for products with guarantees:

- Risk indicator should not be based on historical volatility, because otherwise even positive deviations from the mean value would be considered as risks.
- Historical values on their own do not have any real impact on the future performance and, therefore, do not allow any conclusions on the future risk of long-term products.

### VaR does not sufficiently differentiate between different products

Another major drawback of both methods is that they cannot differentiate sufficiently well between different products. This is mainly due to the fact that for products with downside safeguards the VaR will yield the same result:

- The interval of 2.5% is too narrow to assess the risk of a product from consumer's perspective. Usually, consumers are interested in a more general event than the loss in the single 2.5%-worst case.
- VaR does not differentiate between different (average) losses of different products in negative scenarios, since it does not take into account the skewness of the distribution. Thus, products with different underlying structure (such as e.g. guaranteed products with different underlyings) will be automatically judged in an identical manner.

For example, most consumers interested in life insurance products, see it as a risk that they only receive their contributions back at maturity. For instance, for many traditional products with a guaranteed positive interest rate this probability is zero since the consumers always receive more than this. On the other hand, for a textbook CPPI this probability is relatively high. But in good/bad scenarios the CPPI will perform better/worse than a traditional product. It is important that consumers understand this trade-off.

#### *Example 2:*

*We consider two different CPPIs (Constant Proportion Portfolio Insurance): Both are equipped with a money-back guarantee and provide this guarantee by rebalancing a "risky" and a "risk-free" asset (e.g. money market or fixed income). However, the products differ in the risky asset:*

- *CPPI A invests in Category II underlyings with annualised volatility <0.5%.*

- *CPPI B invests in Category II underlyings with annualised volatility >25%.*

*Considering the risky assets only, common sense would potentially assign CPPI B as being more risky than CPPI A. However, if we apply the VaR at a 2.5% confidence level, it is also very likely that due to the included money-back guarantee, both CPPIs will yield the same VaR and, hence, both CPPIs will be assigned the same risk category. This is due to the fact that VaR at 2.5% will reflect the guarantee and not the different risk of the respective underlying (cf. question 4). Thus, consumers will not understand the different impact of the risky assets and will wrongly judge the products as equally risky.*

Another example is a product with a guarantee less than 100% of the paid-in contributions (e.g. 95%). Applying the VaR, this product will follow a different benchmark and could be automatically assigned to a higher risk class, even when the quantitative differences between such a product and a product with the guaranteed paid-in contributions could be marginal.

Finally, we would like to stress the increasing importance of this issue. As EIOPA states in its current consumers trend report<sup>1</sup>, innovation creates new opportunities for consumers as well as for insurance undertakings. For example, insurance undertakings increasingly offer their customers life insurance products with reduced guarantees in order to achieve better participation in upward markets. Thus, it is of utmost importance that the methodology can robustly differentiate between different products in a meaningful way. This is also important if the basis of this methodology was to be used for other products such as the Pan-European Personal Pension Product (PEPP).

#### Expected Loss for a given Value-at-Risk should be used as a risk measure

As described above, the VaR is not a suitable tool to determine the risk of a PRIIP:

- It only tells us some point-estimate of the loss distribution and not which amount of loss might actually happen when some critical threshold has been breached<sup>2</sup>.

<sup>1</sup> EIOPA Fourth Consumer Trends Report, EIOPA-BoS-15-233

<sup>2</sup> Danielsson, J., Embrechts, P., Goodhart, C., Keating, C., Muennich, F., Renault, O. and Shin, H. (2001). An Academic Response to Basel II. Available at <http://www.lse.ac.uk/fmg/documents/specialPapers/2001/sp130.pdf>

- It tells us only about a loss that occurs with a very low probability.
- It does not say anything about the average loss in certain worst cases.
- It is not robust since products can be constructed where the (overall the same) risk is shifted further in the tail wrongly suggesting low risk of a product.

Therefore, Expected Loss for a given Value-at-Risk is a more appropriate measure for the market risk since it presents an average of the expected loss in the worst case. CTE (conditional tail expectation), which is a very similar measure, might also be considered as a suitable risk measure, for instance the average of the 10% or 20% worst economic scenarios. CTE is numerically very stable for many product categories, especially insurance-based investment products, and easy to explain to retail investors. Thus, it meets the requirements of a risk/reward indicator quite well.

#### Forward-looking probabilistic modelling is suitable for all investment products

An approach based on forward-looking probabilistic modelling should be considered instead for determining the market risk of a product. The GDV would like to stress the following features of a forward-looking model which should be taken into account:

- a model should be based on a few relevant asset classes, in particular bonds, equities;
- it should be based on Monte Carlo and known and well-established capital market models;
- maturity should be taken as the default holding period.

Instead of using fixed buckets as they are used for the UCITS SRRI, a more robust system should be chosen, for instance by taking some reference products generated by taking different mixtures of the assets from the model. These may then serve as a benchmark. This works well in differentiating between the empirical clusters that are seen in the market. Furthermore, this method is very robust with respect to realistic parameter changes.

If model and parameters are prescribed, it is very hard to undermine the method. No market values are needed, i.e. this method also works well for products which are not traded on the market or which are completely new. All product features/mechanisms can be taken into account in the simulation. Distributions can be generated for all kinds of PRIIPs, but it might be necessary to add further risk factors.

Such a model is being developed in Germany for the so-called Rürup and Riester pensions, (which are provided not only by insurers but also funds and banks) by an independent entity „Produktinformationsstelle Altersvorsorge gGmbH“<sup>1</sup>.

A two-level risk indicator is preferable.

In many Member States it is common that some life insurance products offer guarantees, which guarantee at least the sum of the contributions at maturity or even more. If the “first level“ indicator differentiated products e.g. according to the guarantee/protection level, a “second level“ indicator could discriminate amongst product types with regard to the probability of the consumer only receiving paid-in contributions and not more. The probability of having a higher return is strongly correlated to it. Thus, consumers need to decide which risk/reward profile meets their requirements.

For such products a two-level indicator gives consumers the possibility to differentiate between different guarantee mechanisms. It is more accurate, robust and reliable than any qualitative indicators.

**Question 4**

**Would you favour a different confidence interval to compute the VaR? If so, please explain which confidence interval you would use and state your reasons why.**

VaR does not sufficiently differentiate between different products

As described above in the answer to Question 3, the VaR is not a suitable tool to determine the market risk of a PRIIP:

- It only tells us some point-estimate of the loss distribution and not which amount of loss might actually happen when some critical threshold has been breached<sup>2</sup>.
- It tells us only about a loss that occurs with a very low probability. Usually, consumers are interested in a more general event than the loss in the single 2.5%-worst case.
- It does not differentiate between different (average) losses of different products in negative scenarios, since it does not take into account the skewness of the distribution. Thus, products with different underlying

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<sup>1</sup> <http://www.produktinformationsstelle.de/>

<sup>2</sup> Danielsson, J., Embrechts, P., Goodhart, C., Keating, C., Muennich, F., Renault, O. and Shin, H. (2001). An Academic Response to Basel II. Available at <http://www.lse.ac.uk/fmg/documents/specialPapers/2001/sp130.pdf>

structure (such as e.g. guaranteed products with different underlyings) will be automatically judged in an identical manner.

- It is not robust since products can be constructed where the (overall the same) risk is shifted further in the tail wrongly suggesting low risk of a product.

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Another example is a product with a guarantee less than 100% of the paid-in contributions (e.g. 95%). Applying the VaR, this product will follow a different benchmark and could be automatically assigned to a higher risk class, even when the quantitative differences between such a product and a product with the guaranteed paid-in contributions could be marginal.

Finally, we would like to stress the increasing importance of this issue. As EIOPA states in its current consumers trend report<sup>1</sup>, innovation creates new opportunities for consumers as well as for insurance undertakings. For example, insurance undertakings increasingly offer their customers life insurance products with reduced guarantees in order to achieve better participation in upward markets. Thus, it is of utmost importance that the methodology can robustly differentiate between different products in a

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meaningful way. This is also important if the basis of this methodology was to be used for other products such as the Pan-European Personal Pension Product (PEPP).

#### Expected Loss for a given Value-at-Risk should be used as a risk measure

As described above, the VaR is not a suitable tool to determine the risk of a PRIIP:

- It only tells us some point-estimate of the loss distribution and not which amount of loss might actually happen when some critical threshold has been breached<sup>1</sup>.
- It tells us only about a loss that occurs with a very low probability.
- It does not say anything about the average loss in certain worst cases.
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Therefore, Expected Loss for a given Value-at-Risk is a more appropriate measure for the market risk since it presents an average of the expected loss in the worst case. CTE (conditional tail expectation), which is a very similar measure, might also be considered as a suitable risk measure, for instance the average of the 10% or 20% worst economic scenarios. CTE is numerically very stable for many product categories, especially insurance-based investment products, and easy to explain to retail investors. Thus, it meets the requirements of a risk/reward indicator quite well.

#### Risk-free rate of return yields wrong results

Our understanding is that a “risk-neutral” pricing environment assuming a risk-neutral probability measure shall be assumed for deriving the “real-world” VaR or some equivalent annual volatility under the original probability measure.

Hence, potential risk premiums for different asset classes (i.e. the assumption of an expected return above the risk-free rate) are not considered. Instead, one applies a methodology that is originally only valid within a pricing exercise, e.g. for valuation of an option. However, the current approach derives a quantile of these discounted values which is in our opinion a flawed approach. It might produce meaningful results for “vanil-

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<sup>1</sup> Danielsson, J., Embrechts, P., Goodhart, C., Keating, C., Muennich, F., Renault, O. and Shin, H. (2001). An Academic Response to Basel II. Available at <http://www.lse.ac.uk/fmg/documents/specialPapers/2001/sp130.pdf>

la” investment vehicles such as pure equity funds, it is however likely to produce “very wrong” results when more complex structures such as path-dependent CPPIs or similar are considered.

Therefore, we strongly recommend not to analyse quantiles of probability distributions assuming a risk-neutral pricing measure. One cannot use a probability measure designed for pricing – where the only economically relevant figures are expectations of discounted cash-flows – to compute and classify a risk-related number in terms of a probability distribution’s quantile or conditional tail value at risk.

#### **Question 5**

**Are you of the view that the existence of a compensation or guarantee scheme should be taken into account in the credit risk assessment of a PRIIP? And if you agree, how would you propose to do so?**

#### Compensation or guarantee schemes mitigate credit risk

It is of utmost importance that insurance guarantee schemes are taken into account as a risk mitigating factor. First, it contradicts previous views of the ESAs, where it is stated that “Credit risk could be mitigated in some situations such as when there is a guarantee or a compensation scheme (such as the deposit compensation scheme) in place or when appropriate collateral is provided.”<sup>1</sup> Second, from the point of view of the retail investors, the credit risk they are facing is that they could lose money in case of the insolvency of the PRIIP manufacturer. Therefore, if the PRIIP manufacturer is secured through a guarantee scheme, then the credit risk from the point of view of the retail investor is immaterial and the PRIIP should receive CR1.

#### Precedence of consumers’ claims mitigates credit risk

Furthermore, not only are some insurers protected by the insurance guarantee schemes, insurance claims also take precedence over other claims against the insurance undertaking (Solvency II, Article 275(1)(a)). To ensure this, part of the assets of an insurance undertaking serves as security for the claims of the policyholders in case of insurer’s insolvency. Special legal restrictions apply to these assets to ensure that sufficient assets are kept safe in an event of insolvency in order to satisfy the claims of the pol-

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<sup>1</sup> Technical Discussion Paper „Risk, Performance Scenarios and Cost Disclosures In Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs)”, JC DP 2015 01, 23 June 2015

icyholders. Although we understand that ESAs take this mechanism into account in point 65 on page 42, an explicit reference to Solvency II provisions needs to be included.

#### **Question 6**

**Would you favour PRIIP manufacturers having the option to voluntarily increase the disclosed SRI? In which circumstances? Would such an approach entail unintended consequences?**

##### The manufacturers should not be able to increase the SRI

The question itself shows that the risk indicator is neither robust nor stable. To ensure consumer protection, it is of utmost importance that the methodology for the risk indicator yields a number that is robust and stable for different products and ensures legal certainty for manufacturers. A manufacturer choice to adjust the risk indicator will hinder comparability. Furthermore, since risk is closely linked to reward, an arbitrary increase would wrongly suggest that the product has better performance chances.

That is also why the risk indicator should include a disclaimer indicating that higher risk is typically related to higher rewards for manufacturers that have low credit risk.

#### **Question 7**

**Do you agree with an adjustment of the credit risk for the tenor, and how would you propose to make such an adjustment?**

##### Guarantee schemes and precedence of consumers' claims mitigate credit risk

The credit risk of a product does not necessarily increase with an increasing term of a product. The risk is not increased if consumers' claims

- are protected through an insurance guarantee scheme or
- take precedence over other claims against the insurance undertaking and are kept in a segregated account

First, insurance guarantee schemes should be taken into account as a risk mitigating factor. It contradicts previous views of the ESAs, where it is stated that "Credit risk could be mitigated in some situations such as when there is a guarantee or a compensation scheme (such as the deposit compensation scheme) in place or when appropriate collateral is provid-

ed."<sup>1</sup> From the point of view of the retail investors, the credit risk they are facing is that they could lose money in case of the insolvency of the PRIIP manufacturer. Therefore, if the PRIIP manufacturer is secured through a guarantee scheme, then the credit risk from the point of view of the retail investor is immaterial and the PRIIP should receive CR1.

Second, not only are some insurers protected by the insurance guarantee schemes, insurance claims also take precedence over other claims against the insurance undertaking (Solvency II, Article 275(1)(a)). To ensure this, part of the assets of an insurance undertaking serves as security for the claims of the policyholders in case of insurer's insolvency. Special legal restrictions apply to these assets to ensure that sufficient assets are kept safe in an event of insolvency in order to satisfy the claims of the policyholders. Although we understand that ESAs take this mechanism into account in point 65 on page 42, an explicit reference to Solvency II provisions needs to be included.

#### Mechanical overreliance upon ratings should be avoided

Finally, as rightly pointed out by the ESAs, overreliance upon credit rating agencies should be avoided. Furthermore, not all manufacturers have a credit rating. Thus, small and medium-size entities will be automatically at competitive disadvantage. Therefore, the use of credit ratings has many essential drawbacks and should be avoided if possible.

#### **Question 8**

**Do you agree with the scales of the classes MRM, CRM and SRI? If not, please specify your alternative proposal and include your reasoning.**

#### Consistent methodology for the risk indicator should be the biggest priority

First of all, a meaningful methodology for the risk indicator that enables stable, robust and transparent comparison of different products is necessary before the fine-tuning of aggregation of different risks is performed. The current methodology, especially for Category IV PRIIPs is too vague and leaves many factors up to manufacturers' discretion.

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<sup>1</sup> Technical Discussion Paper „Risk, Performance Scenarios and Cost Disclosures In Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs)“, JC DP 2015 01, 23 June 2015

The aggregation methodology is unclear

Furthermore, the methodology behind the aggregation of different market risk classes and credit risk scales into a single SRI is not described in a transparent way. The assignment seems arbitrary. In general, it is important that the chosen methodology is continuous and does not show gaps between issuers with similar creditworthiness.

Finally, the computation of the VaR equivalent volatility is not meaningful.

**Question 9**

**Are you of the opinion that for PRIIPs that offer a capital protection during their whole lifespan and can be redeemed against their initial investment at any time over the life of the PRIIP a qualitatively assessment and automatic allocation to MRM class 1 should be permitted?**

**Are you of the opinion that the criteria of the 5 year tenor is relevant, irrespective of the redemption characteristics?**

The choice of a five-year tenor seems arbitrary

Five-year tenor criteria selected by the ESAs seem to be arbitrary and are misleading for retail investors. The five-year tenor was presumably introduced to address inflation concerns. In GDV's view, the impact of inflation on the value of the PRIIP should not affect the market risk mainly because inflation is not a risk inherent for PRIIPs but affects all investment products in the same way. In addition, this feature is not included in pre-contractual information disclosure for other products (UCITS for instance). Therefore, this distinction is neither helpful for retail investors nor does it increase comparability or transparency of products.

Furthermore, the market risk of insurance-based investment products is even reduced in the long term through smoothing mechanisms such as diversification of assets, collective investment and pooling of market risk.

Same methodology for the market risk should apply to all PRIIPs

The same methodology should apply to all PRIIPs to ensure consistency and comparability, which is one of the main aims of the PRIIPs Regulation. Moreover, manufacturers will have to implement several burdensome methods for different products.

### **Question 10**

**Are you aware of other circumstances in which the credit risk assessment should be assumed to be mitigated? If so, please explain why and to what degree it should be assumed to be mitigated?**

#### Precedence of consumers' claims mitigates credit risk

It is of utmost importance that if claims of policyholders take precedence over other claims, then it should be regarded as a risk-mitigating factor. This is the case for insurance undertakings that fall under the scope of the Solvency II Directive (Solvency II, Article 275(1)(a)). To ensure this, part of the assets of an insurance undertaking serves as security for the claims of the policyholders in case of insurer's insolvency. Special legal restrictions apply to these assets to ensure that sufficient assets are kept safe in an event of insolvency in order to satisfy the claims of the policyholders. This should warrant allocation to credit risk class 1.

#### Compensation or guarantee schemes mitigate credit risk

Insurance guarantee schemes should be taken into account as a risk mitigating factor. It contradicts previous views of the ESAs, where it is stated that "Credit risk could be mitigated in some situations such as when there is a guarantee or a compensation scheme (such as the deposit compensation scheme) in place or when appropriate collateral is provided."<sup>1</sup> From the point of view of the retail investors, the credit risk they are facing is that they could lose money in case of the insolvency of the PRIIP manufacturer. Therefore, if the PRIIP manufacturer is secured through a guarantee scheme, then the credit risk from the point of view of the retail investor is immaterial and the PRIIP should receive CR1.

### **Question 11**

**Do you think that the look through approach to the assessment of credit risk for a PRIIP packaged into another PRIIP is appropriate?**

The look through approach should apply only if consumers bear the credit risk of the underlying. However, for insurance-based investment products the opposite is often true.

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<sup>1</sup> Technical Discussion Paper „Risk, Performance Scenarios and Cost Disclosures In Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs)“, JC DP 2015 01, 23 June 2015

In general, credit risk seems to be much more relevant for non-insurance-based investment products. Furthermore, it is important that risk-mitigating factors such as existence of an insurance guarantee scheme and precedence of policyholders' claims are taken into account and warrant allocation to credit risk class 1.

#### **Question 12**

**Do you think the risk indicator should take into account currency risk when there is a difference between the currency of the PRIIP and the national currency of the investor targeted by the PRIIP manufacturer, even though this risk is not intrinsic to the PRIIP itself, but relates to the typical situation of the targeted investor?**

#### **Question 13**

**Are you of the opinion that the current Consultation Paper sufficiently addresses this issue? Do you think it is made sufficiently clear that the value of a PRIIP could be significantly less compared to the guaranteed value during the life of the PRIIP? Several alternatives are analysed in the Impact Assessment under policy option 5: do you see any additional analysis for these assessment?**

Only single risk indicator for a realistic term of a product is meaningful for consumers

The PRIIPs Regulation states that there is a single risk indicator (Article 8(3)(d)). This is to be a summary indicator, which takes account of and combines the relevant factors. Thus, the presentation of several risk indicators for different intermediate stages as suggested in option 5.2 would be contrary to the Level 1 text. The limitation of the risk indicator should also be explained. In our view, a reference to the boundaries of the risk indicator is sufficient.

Furthermore, according to the PRIIPs Regulation, the KID includes an entire section for the description of what happens if consumers take out money early (Article 8(3)(g)(iv)). Thus, this section provides information for the consumer about what happens when they surrender early. If the same information is included differently in different sections, this would only lead to confusion.

The same arguments apply to the option 5.1. Consumers will be confused if the term for the risk indicator is shorter than the term of the product displayed in Article 8(3)(d). Moreover, a risk indicator based on a short and standardised holding period for all products is not meaningful since for long-term products, such as insurance-based investment products, consumers will receive a wrong impression about the real risk of the product.

#### **Question 14**

**Do you agree to use the performance fee, as prescribed in the cost section, as a basis for the calculations in the performance section (i.e. calculate the return of the benchmark for the moderate scenario in such a way that the return generates the performance fee as prescribed in the cost section)? Do you agree the same benchmark return should be used for calculating performance fees for the unfavourable and favourable scenarios, or would you propose another approach, for instance automatically setting the performance fees to zero for the unfavourable scenario? Please justify your proposal.**

#### **Question 15**

**Given the number of tables displayed in the KID and the to a degree mixed consumer testing results on whether presentation of performance scenarios as a table or a graph would be most effective, do you think a presentation of the performance scenarios in the form of a graph should be preferred, or both a table and a graph?**

#### Intermediate values and graphs are misleading for consumers

The proposed performance scenarios contradict the provisions of the Regulation on the structure of the KID. For products with a fixed term, the Regulation envisages the KID to describe the characteristics of the PRIIP under the assumption that the regular term is adhered to. For this reason, the term of the product is prominently specified in the section titled 'What is this product?'. The retail investor will, therefore, take into account the regular holding period when considering the information on risk, costs and performance of the product. Explanations on the consequences of cashing in before the end of the term are supposed to be provided under the section which was specifically created for this purpose: 'How long should I hold it and can I take money out early? Therefore, intermediate values of the product should be included in the section on surrender value of the product.

Furthermore, the information on intermediate values, especially presented in a graph, would mislead consumers: For insurance-based investment products, intermediate values are not the same as final values of a product with a shorter holding period, i.e. the value after 15 years of a product with a term of 30 years is not the same as the final value of a product with a term of 15 years. In any case, it is of utmost importance that this is explained to the consumer in a narrative manner.

#### Details of performance scenarios should be prescribed at EU level

As regards performance scenarios in general, we regret the fact that too many details might be left up to manufacturers' discretion. The GDV believes that performance scenarios should be prescribed. Otherwise, it can neither be guaranteed that the chosen scenarios are reasonable nor that different products can be compared, which is one of the aims of the PRIIPs Regulation. Moreover, only prescribed scenarios ensure legal certainty for the PRIIPs manufacturers. The guidelines proposed by the ESAs should solve these issues.

#### Performance scenarios should indicate the uncertainty of returns only

While performance scenarios can be used as an indication for the real future return for short-term products, it would be impossible but also irresponsible by manufacturers to state the exact performance in the very long term. In our view, a main goal of the performance scenarios is to indicate that the exact performance of the product is not certain. Therefore, in our view the assignment of the terms "positive", "moderate" and "negative" is not appropriate for long-term products provided that consumer testing has shown that consumers tend to read an implied probability of the outcomes even if no information was provided on how probable the scenarios were.

A same pre-determined pool of scenarios for different risk/reward classes, or some reference values, if applicable, should be used instead. By doing so, the higher risk products should have a larger number and a wider range of scenarios. If there is no reference value, an even number of scenarios is preferable since otherwise the scenario in the middle is often misinterpreted by retail investors to be the most likely one. The growth rates used, however, should not vary for each risk/reward class since this would impede comparability.

#### Performance scenarios should be forward-looking

Since it is often not possible to find suitable historical data for new products, especially for products with very long terms, performance scenarios should be forward-looking.

In this context, the German insurers would like to repeat their message that the information on past performance is misleading for consumers: First, on their own, they do not give any indication regarding potential future performances, especially for long-term products. Second, consumers tend to draw too many conclusions from past performances.

#### Death benefits should not be presented in performance scenarios

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

#### A delay in the PRIIPs timeline is needed also for the guidelines

Finally, regarding the proposed guidelines we would like to point to the extremely short time line for the Level 2. If the specifications for performance scenarios are published at a later stage, it will leave manufacturers even less time to implement the provisions. Thus, a delay of the PRIIPs Regulation is indispensable for manufacturers and for consumers who need to be able to rely on the information provided. In any case, the guidelines should be developed as soon as possible and in any case before the application of the PRIIPs Regulation.

In terms of regulation, regulatory technical standards are always to be preferred to guidelines. They establish directly binding uniform implementation standards and prevent “gold plating” when respective provisions are being implemented at national level.

#### **Question 16**

**Do you agree with the scope of the assets mentioned in paragraph 25 of Annex VI on transaction costs for which this methodology is prescribed? If not, what alternative scope would you recommend?**

Methods for investments funds should not be copy pasted to insurance products

For life insurance products, methods that already exist for these products should be used instead.

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

Second, life insurers provide long-term products, resulting in the fact that the investments of life insurers are mainly long-term oriented, so the assets in their portfolios have often mid- to long-term maturities. Thus, the frequency of reallocation is relatively rare compared to other PRIIPs. As a result, implicit transaction costs are marginal, negligible and without relevance for retail investors.

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

#### **Question 17**

**Do you agree with the values of the figures included in this table? If not, which values would you suggest? (please note that this table could as well be included in guidelines, to allow for more flexibility in the revision of the figures)**

#### Methods for investments funds should not be copy pasted to insurance products

For life insurance products, methods that already exist for these products should be used instead.

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

Second, life insurers provide long-term products, resulting in the fact that the investments of life insurers are mainly long term oriented, so the as-

sets in their portfolios have often mid- to long-term maturities. Thus, the frequency of reallocation is relatively rare compared to other PRIIPs. As a result, implicit transaction costs are marginal, negligible and without relevance for retail investors.

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

#### **Question 18**

**Do you agree that the monetary values indicated in the first table are a sum of costs over the respective holding periods? Or should the values reflect annualized amounts? If you prefer annualized amounts, which method for annualisation should be used (e.g. arithmetic average or methods that consider discounting effects)?**

Only annualised amounts ensure comparability and comprehensibility

For the comparability of products and level playing field of manufacturers annualised costs should be presented together with the Reduction in Yield indicator. A presentation of the total costs for the whole investment period

- would not allow for an effective comparison between products with different terms,
- would make a product with a longer term automatically look more expensive – even if it is cheaper – than a product with a shorter term,
- would be misleading for consumers that compare products with different terms and investment amounts since the total costs in monetary terms cannot be linearly scaled.

Furthermore, it could even happen that the total costs of a single-premium product with a good net yield for consumer could be higher than the total investment if the term of a product is sufficiently long. The information on the sum of costs would be nothing but misleading for consumers.

As regards the method of annualisation, it is important that compound interest effect is taken into account. Therefore, methods that consider discounting effects should be applied.

### **Question 19**

**Do you think that estimating the fair value of biometric risk premiums as stated in paragraph 55(b) of Annex VI would raise any technical or practical difficulties?**

#### Biometric risk premium is not a cost

The GDV welcomes that the ESAs acknowledge that the aggregation of the investment costs and the full biometric risk premium would be inappropriate. In our view, such an aggregation would (1) not seem to be in line with the level 1 text of the PRIIPs Regulation; (2) not be in the interest of consumers who will not be in a position to compare what is comparable; and (3) create an unlevel playing field for insurance-based investment products.

First of all, the GDV would like to point out that it believes that it is not appropriate to include the biometric risk premium in the costs section of the KID. Since retail investors receive insurance benefits for these payments, the biometric risk premium should be deemed a “price” rather than a cost.

#### Consumers should be able to compare investments

Recital 15 of the PRIIPs Regulation states that “retail investors should be provided with the information necessary for them to make an informed investment decision and compare different PRIIPs [...]” Biometric risk premiums are not linked to the costs of the investment element of life insurance contracts and policyholders get benefit payments from insurance cover in return that do not exist for other types of PRIIPs. The consumer’s decision, however, would be distorted if costs for the actual savings process include costs/premiums which do not relate to the savings process and for which the customer receives additional benefits.

Separating fair value and costs as suggested by the ESAs is in our view a fall-back solution since this separation is difficult to understand for the retail investor and prohibits the comparison of investment costs. However, it should be noted that the difference between the fair value and the total premium is not the costs but the volatility adjustment.

#### Additional death benefits should be described in “What is this product?” section

If additional death benefits above the minimum and/or additional risk benefits can be concluded, they should be included in the section titled “What is this product?” (Article 8(3)(c)(iv) of the PRIIPs Regulation) as

qualitative information. This purely qualitative approach also has an extra benefit of reducing the amount of KIDs to be produced to a manageable amount: if a high death premium or additional benefits were to be quantified, different KIDs would be necessary for many other factors such as age, occupation, state of health, (dangerous) hobbies, etc., thus adding unnecessary complexity to the KID. In the representation suggested by the GDV, the only varying factor would be the different maturities of the product.

#### Separate pure risk riders should be excluded from the KID

The ESAs have already pointed out correctly in the previous consultation that a separate risk-rider could as well be offered as separate contract that would not fall under the PRIIPs Regulation and where no investment element would be associated with a risk rider. Therefore, the information on these benefits should not be included in the KID.

#### **Question 20**

**Knowing that the cost element of the biometric risk premium is included in the total costs calculation, how do you think the investor might be most efficiently informed about the other part of the biometric risk premium (i.e. the fair value), and/or the size of biometric risk premium overall? Do you consider it useful to include the fair value in a separate line in the first table, potentially below the RIY? Or should information on the fair value be disclosed in another part of the KID (for instance, the “What is this product?” section, where the draft RTS currently disclose biometric risk premiums in total, and/or in the performance section)? What accompanying narrative text do you think is needed, and where should this be placed, including specifically narrative text in the cost section?**

#### Cost section of the KID deals with investment costs

First, it seems key to recall that the Level 1 text of the PRIIPs Regulation (Article 8(f)) introduces in the KID a section on costs which should include “the costs associated with an investment in the PRIIP” – it does not say “costs associated with an investment and biometric protection”. Therefore, separating the full biometric risk premium and the investment cost, as well as being the most transparent and meaningful approach, is also in line with the level 1 text.

Second, Recital 15 of the PRIIPs Regulation states that “retail investors should be provided with the information necessary for them to make an informed investment decision and compare different PRIIPs [...]” Biometric risk premiums are not linked to the costs of the investment element of life insurance contracts and policyholders get benefit payments from insurance cover in return that do not exist for other types of PRIIPs. The consumer’s decision, however, would be distorted if costs for the actual savings process include costs/premiums which do not relate to the savings process and for which the customer receives additional benefits.

Full biometric risk premium should be displayed in the “What is this product?” section

Since retail investors receive insurance benefits for these payments, the total biometric risk premium should be deemed a “price” rather than a cost. This price should be displayed – alongside with the total price of the PRIIP – only in the “What is this product?” section of the PRIIPs KID.

Separating fair value and costs as suggested by the ESAs is in our view a fall-back solution since this separation is difficult to understand for the retail investor and prohibits the comparison of investment costs. In our view it is clear and straightforward that the fair value should be displayed in the “What is this product?” section of the PRIIPs KID, if at all.

#### **Question 21**

**Given evidence as to the difficulties consumers may have using percentage figures, would you prefer an alternative presentation of the second table, solely using monetary values instead? As with the first table, please also explain what difficulties you think might arise from calculating monetary values, and whether this should be on an annualized basis, and if so, how?**

RIY together with annualised costs are concise, comprehensible and comparable

First, we would like to point out that the comparability of monetary values and their comprehensibility for consumers are problematic and not the calculation itself. If the total costs in monetary terms are presented, then it

- would not allow for an effective comparison between products with different terms,
- would make a product with a longer term automatically look more expensive – even if it is cheaper – than a product with a shorter term,

- would be misleading for consumers that compare products with different terms since the total costs in monetary terms cannot be linearly scaled.

Furthermore, it could even happen that the total costs of a single-premium product with a good net yield for consumer could be higher than the total investment if the term of a product is sufficiently long. The information on the sum of costs would be nothing but misleading for consumers.

Therefore, in order to ensure comparability of products and better comprehensibility for consumers, the following cost figures should be displayed:

- RIY for the holding period of the contract, which shows the total impact of costs in percent and includes all costs: direct and indirect, one-off and recurring costs;
- annualised total costs in monetary terms.

#### Information overload and complexity of costs representation should be reduced

We would like to point to the contradiction in the visual representation of the risk class and costs of PRIIPs. We welcome the fact that the risk indicator suggested by the ESAs includes only one number corresponding to the total risk of the product and is easy to grasp for retail investors. Unfortunately, the opposite is true for the representation of costs: the ESAs suggest two tables which not only exceed the requirements of the level 1 text but also include 15 numbers in the first table and five numbers in the second table. The comprehensibility of such information is highly questionable since consumer testing has shown that a higher level of detail often results in a worse performance of retail investors. The most important information – which costs a consumer will bear if he holds the product up to maturity, which are displayed through RIY and annualised total costs in monetary terms at maturity – is almost impossible to find. The visual focus is wrongly on the first years of the contract and not on the holding period intended by the consumer.

Furthermore, we believe that a high level of detail will decrease comprehensibility for consumers in general: if the recurring costs of product A are higher in the first intermediate stage and lower in the second intermediate stage than the respective costs of product B with incidental costs of product A being lower in the first stage and higher in the second stage, then which product shall the consumer buy?

#### Intermediate values in the costs section are misleading for consumers

The proposed representation of the costs contradicts the provisions of the Regulation on the structure of the KID. For products with a fixed term, the Regulation envisages the KID to describe the characteristics of the PRIIP under the assumption that the regular term is adhered to. For this reason, the term of the product is prominently specified in the section titled 'What is this product?'. Therefore, the retail investor will take into account the regular holding period when considering the information on risk and costs of the product. Explanations on the consequences of cashing in before the end of the term are supposed to be provided under the section which was specifically created for this purpose: 'How long should I hold it and can I take money out early?'. Therefore intermediate values of the product should be included in the section on surrender value of the product. Furthermore, the information on the costs for early stages of the contract will wrongly present possibly cheaper products with non-linear cost structure as more expensive than products with a linear cost structure. Finally, the information on intermediate stages is misleading. For insurance-based investment products intermediate values are not the same as final values of a product with a shorter holding period, i.e. the value after 15 years of a product with a term of 30 years is not the same as the final value of a product with a term of 15 years.

#### Intermediate values should be included in the section on surrender value

In order to ensure full transparency, the Regulation text dedicates an entire section of the PRIIPs KID to the surrender value of the product. Thus, this section provides information for the consumers about what happens when they surrender early. In our view, this section should include the "surrender value/sum of contributions" ratio and should at least be presented for e.g. 1, 5, 10, 20 and 30 years. If the same information is included differently in different sections, this would only lead to confusion.

#### **Question 22**

**Given the number of tables shown in the KID, do you think a more graphic presentation of the breakout table should be preferred?**

#### Information overload and complexity of costs representation should be reduced

We would like to point to the contradiction in the visual representation of the risk class and costs of PRIIPs. We welcome the fact that the risk indicator suggested by the ESAs includes only one number corresponding to

the total risk of the product and is easy to grasp for retail investors. Unfortunately, the opposite is true for the representation of costs: the ESAs suggest two tables which not only exceed the requirements of level 1 text but also include 15 numbers in the first table and five numbers in the second table. The comprehensibility of such information is highly questionable since consumer testing has shown that a higher level of detail often results in a worse performance of retail investors. The most important information – which costs a consumer will bear if he holds the product up to maturity, which are displayed through RIY and annualised total costs in monetary terms at maturity – is almost impossible to find. The visual focus is wrongly on the first years of the contract and not on the holding period intended by the consumer.

#### RIY together with annualised costs are concise, comprehensible and comparable

The German insurers firmly believe that the Reduction in Yield provides consumers with a simple and understandable figure and enables them to compare different products in a uniform, robust and consistent way. Moreover, RIY is the most relevant figure for the consumers since it shows the total impact of costs and takes all costs into account. Therefore, it is important that RIY is visually highlighted in the costs section. In our view, prominent presentation of RIY and total annualised costs in monetary terms is more suitable than (more or less) graphic presentation of the breakout table. Such a presentation would also agree with a simple visual presentation of risk.

#### Intermediate values in the costs section are misleading for consumers

The proposed representation of the costs contradicts the provisions of the Regulation on the structure of the KID. For products with a fixed term, the Regulation envisages the KID to describe the characteristics of the PRIIP under the assumption that the regular term is adhered to. For this reason, the term of the product is prominently specified in the section titled 'What is this product?'. Therefore, the retail investor will take into account the regular holding period when considering the information on risk and costs of the product. Explanations on the consequences of cashing in before the end of the term are supposed to be provided under the section which was specifically created for this purpose: 'How long should I hold it and can I take money out early? Therefore intermediate values of the product should be included in the section on surrender value of the product. Furthermore, the information on the costs for early stages of the contract will wrongly present possibly cheaper products with non-linear cost structure

as more expensive than products with a linear cost structure. Finally, the information on intermediate stages is misleading. For insurance-based investment products intermediate values are not the same as final values of a product with a shorter holding period, i.e. the value after 15 years of a product with a term of 30 years is not the same as the final value of a product with a term of 15 years.

Intermediate values should be included in the section on surrender value

In order to ensure full transparency, the Regulation text dedicates an entire section of the PRIIPs KID to the surrender value of the product. Thus, this section provides information for the consumers about what happens when they surrender early. In our view, this section should include the “surrender value/sum of contributions” ratio and should at least be presented for, say, 1, 5, 10, 20 and 30 years. If the same information is included differently in different sections, this would only lead to confusion.

**Question 23**

**The example presented above includes a possible way of showing the variability of performance fees, by showing the level for all three performance scenarios in the KID, highlighting the ‘moderate’ scenario, which would be used for the calculation of the total costs. Do you believe that this additional information should be included in the KID?**

The scenarios should be prescribed

Otherwise the calculation of costs will be arbitrary and no comparability of different products will be ensured.

Furthermore, as stated in question 15, if there is no reference value, an even number of scenarios is preferable since otherwise the scenario in the middle is often misinterpreted by retail investors to be the most likely one. This misinterpretation could be increased by the highlighting of the moderate scenario.

**Question 24**

**To reduce the volume of information, should the first and the second table of Annex VII be combined in one table? Should this be supplemented with a breakdown of costs as suggested in the graphic above?**

### Information overload and complexity of costs representation should be reduced

In our view, this option will not solve the actual problem of information overload regarding costs. The German insurers wonder how consumer testing could possibly lead to such a contradiction in the visual representation of the risk class and costs of PRIIPs. We welcome the fact that the risk indicator suggested by the ESAs includes only one number corresponding to the total risk of the product and is easy to grasp for retail investors. Unfortunately, the opposite is true for the representation of costs: the ESAs suggest more than 20 different values for costs. The comprehensibility of such information is highly questionable since consumer testing has shown that a higher level of detail often results in a worse performance of retail investor. The most important information – which costs a consumer will bear if he holds the product up to maturity, which are displayed through RIY and annualised total costs in monetary terms at maturity – is almost impossible to find. The visual focus is wrongly on the first years of the contract and not on the holding period intended by the consumer.

### RIY together with annualised costs are concise, comprehensible and comparable

The German insurers firmly believe that the Reduction in Yield provides consumers with a simple and understandable figure and enables them to compare different products in a uniform, robust and consistent way. Moreover, RIY is the most relevant figure for the consumers since it shows the total impact of costs and takes all costs into account. Therefore, it is important that RIY is visually stressed in the costs section. In our view, prominent presentation of RIY and total annualised costs in monetary terms is more suitable than (more or less) graphic presentation of the breakout table. Such a presentation would also agree with a simple visual presentation of risk.

### Intermediate values in the costs section are misleading for consumers

The proposed representation of the costs contradicts the provisions of the Regulation on the structure of the KID. For products with a fixed term, the Regulation envisages the KID to describe the characteristics of the PRIIP under the assumption that the regular term is adhered to. For this reason, the term of the product is prominently specified in the section titled 'What is this product?'. Therefore, the retail investor will take into account the regular holding period when considering the information on risk and costs of the product. Explanations on the consequences of cashing in before the

end of the term are supposed to be provided under the section which was specifically created for this purpose: 'How long should I hold it and can I take money out early? Therefore, intermediate values of the product should be included in the section on surrender value of the product. Furthermore, the information on the costs for early stages of the contract will wrongly present possibly cheaper products with non-linear cost structure as more expensive than products with a linear cost structure. Finally, the information on intermediate stages is misleading. For insurance-based investment products, intermediate values are not the same as final values of a product with a shorter holding period, i.e. the value after 15 years of a product with a term of 30 years is not the same as the final value of a product with a term of 15 years.

Intermediate values should be included in the section on surrender value

In order to ensure full transparency, the Regulation text dedicates an entire section of the PRIIPs KID to the surrender value of the product. Thus, this section provides information for the consumers about what happens when they surrender early. In our view, this section should include the "surrender value/sum of contributions" ratio and should at least be presented for e.g. 1, 5, 10, 20 and 30 years. If the same information is included differently in different sections, this would only lead to confusion.

**Question 25**

**In relation to paragraph 68 a) of Annex VI: Shall the RTS specify that for structured products calculations for the cost free scenario have always to be based on an adjustment of the payments by the investor?**

Calculations for the cost free scenario should be adjusted

It is necessary that provisions are uniform and comparable. Thus, the GDV agrees that the RTS shall specify that for structured products calculations for the cost free scenario must always be based on an adjustment of the payments by the investor.

The same comparability arguments apply to the method of calculation of the cost-free scenario described in point 68a on page 70 as differing outcomes for the two methods suggested are possible. Thus, the GDV supports the method based on the reduction of gross payments.

#### **Question 26**

**Regarding the first table of the cost section presented in Annex VII, would you favour a detailed presentation of the different types of costs, as suggested in the Annex, including a split between one-off, recurring and incidental costs? Alternatively, would you favour a shorter presentation of costs showing only the total costs and the RIY?**

RIY together with annualised costs are concise, comprehensible and comparable

The German insurers would clearly welcome a shorter, concise presentation of costs showing only the total costs and the RIY. The German insurers firmly believe that the Reduction in Yield provides consumers with a simple and understandable figure and enables them to compare different products in a uniform, robust and consistent way. Moreover, RIY is the most relevant figure for the consumers since it shows the total impact of costs and takes all costs into account. Therefore, it is important that RIY is visually stressed in the costs section. In our view, prominent presentation of RIY and total annualised costs in monetary terms is more suitable than (more or less) graphic presentation of the breakout table. Such a presentation would also enable a simple visual presentation of risk.

Information overload and complexity of costs representation should be reduced

Therefore, we wonder how consumer testing could possibly lead to such a contradiction in the visual representation of the risk class and costs of PRIIPs. We welcome the fact that the look of the risk indicator suggested by the ESAs includes only one number corresponding to the total risk of the product and is easy to grasp for retail investors. Unfortunately, the opposite is true for the representation of costs: the ESAs suggest more than 20 different values for costs. The comprehensibility of such information is highly questionable since consumer testing has shown that a higher level of detail often results in a worse performance of retail investors. The most important information – which costs a consumer will bear if he holds the product up to maturity, which are displayed through RIY and annualised total costs in monetary terms at maturity – is almost impossible to find. The visual focus is wrongly on the first years of the contract and not on the holding period intended by the consumer.

#### Intermediate values in the costs section are misleading for consumers

The proposed representation of the costs contradicts the provisions of the Regulation on the structure of the KID. For products with a fixed term, the Regulation envisages the KID to describe the characteristics of the PRIIP under the assumption that the regular term is adhered to. For this reason, the term of the product is prominently specified in the section titled 'What is this product?'. Therefore, the retail investor will take into account the regular holding period when considering the information on risk and costs of the product. Explanations on the consequences of cashing in before the end of the term are supposed to be provided under the section which was specifically created for this purpose: 'How long should I hold it and can I take money out early?'. Therefore, intermediate values of the product should be included in the section on surrender value of the product. Furthermore, the information on the costs for early stages of the contract will wrongly present possibly cheaper products with non-linear cost structure as more expensive than products with a linear cost structure. Finally, the information on intermediate stages is misleading. For insurance-based investment products intermediate values are not the same as final values of a product with a shorter holding period, i.e. the value after 15 years of a product with a term of 30 years is not the same as the final value of a product with a term of 15 years.

#### Intermediate values should be included in the section on surrender value

In order to ensure full transparency, the Regulation text dedicates an entire section of the PRIIPs KID to the surrender value of the product. Thus, this section provides information for the consumer about what happens when they surrender early. In our view, this section should include the "surrender value/sum of contributions" ratio and should at least be presented for e.g. 1, 5, 10, 20 and 30 years. If the same information is included differently in different sections, this would only lead to confusion.

#### **Question 27**

**Regarding the second table of the cost section presented in Annex VII, would you favour a presentation of the different types of costs showing RIY figures, as suggested in the Annex, or would you favour a presentation of costs under which each type of costs line would be expressed differently, and not as a RIY figure -expressed as a percentage of the initial invested amount, NAV, etc.?**

Information overload and complexity of costs representation should be reduced

In our view, the second table is completely misleading for consumers since the values do not provide an added value. Furthermore, we do not understand the motivation to introduce additional indicators since in our view the suggested presentation is already too complex and not comprehensible for retail investors.

RIY together with annualised costs are concise, comprehensible and comparable

The German insurers would clearly welcome a shorter, concise presentation of costs showing only the total costs and the RIY. The German insurers firmly believe that the Reduction in Yield provides consumers with a simple and understandable figure and enables them to compare different products in a uniform, robust and consistent way. Moreover, RIY is the most relevant figure for the consumers since it shows the total impact of costs and takes all costs into account. Therefore, it is important that RIY is visually stressed in the costs section. In our view, prominent presentation of RIY and total annualised costs in monetary terms is more suitable than (more or less) graphic presentation of the breakout table. Such a presentation would also agree with a simple visual presentation of risk.

#### **Question 28**

**Do you have any comments on the problem definition provided in the Impact Assessment?**

**Are the policy issues that have been highlighted, in your view, the correct ones? If not, what issues would you highlight?**

**Do you have any views on the identified benefits and costs associated with each policy option?**

**Is there data or evidence on the highlighted impacts that you believe needs to be taken into account?**

**Do you have any views on the possible impacts for providers of underlying investments for multi-option products, and in particular indirect impacts for manufacturers of underlying investments used by these products, including where these manufacturers benefit from the arrangements foreseen until the end of 2019 under Article 32 of the PRIIPs Regulation?**

**Are there significant impacts you are aware of that have not been addressed in the Impact Assessment? Please provide data on their scale and extent as far as possible.**

The German insurers are very concerned about the extremely short period provided for the industry to implement the key information document (KID) for PRIIPs.

On the one hand, there will only be 3 to 4 months for the industry to implement the KID. Such a short implementation timeframe is unrealistic. Manufacturers will definitely need more time to develop and implement methods which will result in trustworthy, meaningful, comparable, and stable information for consumers.

On the other hand, some methodologies introduced in the draft RTS – in particular on the risk indicator – are in our view unworkable, incomprehensible, incomparable, and could even lead to misleading information for consumers.

The GDV, therefore, calls for a one-year extension of the PRIIPs implementation deadline in order to give the ESAs enough time to develop better methodology for the customers and to allow the industry to effectively implement the KID.

Furthermore, the GDV would like to highlight its key messages on the policy issues that are reflected throughout the paper.

### **Risk**

- Forward-looking methodology previously suggested in the TDP was a good starting point for the development of a reliable risk indicator that enables a fair comparison of all PRIIPs. It is unclear why the ESAs after having already consulted four different methodologies for the risk indicator now suggest completely new methods.
- The same methodology should apply to all PRIIPs to ensure consistency and comparability, which is one of the main aims of the PRIIPs Regulation. Moreover, manufacturers will have to implement several burdensome methods for different products.
- The bootstrap methodology has severe drawbacks (e.g. it is backward looking) and should not be used for insurance-based investment products. Cornish-Fisher method is also not suitable for products with guarantees.

- Both methodologies suggested cannot differentiate sufficiently well between different products, e.g. between different guarantee mechanisms.
- Expected Loss for a given Value-at-Risk should be used as a risk measure instead of the VaR.
- Insurance guarantee schemes and the precedence of policyholders over other claims should be taken into account as risk-mitigating factors resulting in CR1 when assessing the credit risk of insurers.
- The methods for the risk indicator should be evaluated carefully for different real-world products in order for them to be used by the industry.

### **Costs**

- The total biometric risk premium should be included in the section “What is this product?”. We highly appreciate that the ESAs do not see the biometric risk premium as a cost.
- We welcome the decision to apply the Reduction in Yield (RIY) approach when determining the costs of a product.
- The information overload and complexity of costs representation should be reduced in order to enhance comprehensibility and enable comparability. Short and meaningful presentation of costs should be envisaged.
- The presentation of intermediate values in the costs section is misleading for consumers and should be avoided.
- To ensure both, comparability and a level playing field between manufacturers, only a visually highlighted RIY indicator together with annualised costs in monetary terms should be presented. Only these two figures enable comparability of products with different terms in a meaningful way.

### **Performance scenarios**

- Performance scenarios should be prescribed. Otherwise comparability between different products cannot be ensured.
- Additional guidelines mean less time to implement meaningful, comparable and stable methods for different types of PRIIPs.

Berlin/Brussels, 29 January 2016