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# REPLY FOR THE CONSULTATION PAPER ON PRIIPS KEY INFORMATION DOCUMENTS ORGANISED BY THE EUROPEAN SECURITIES AND MARKETS AUTHORITY

BNP PARIBAS

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# Introduction

BNP Paribas Group (www.bnpparibas.com) is a European leader in banking and financial services, with a significant and growing presence in the United States and leading positions in Asia. The Group has one of the largest international banking networks, with a presence in over 75 countries and nearly 190,000 employees including 147,000 in Europe - among whom 18,000 in Italy, 16,500 in Belgium, 58,000 in France and 3,700 in Luxembourg. BNP Paribas enjoys key positions in Corporate and Investment Banking, Private Banking & Asset Management, Insurance, Securities Services and Retail Banking.

Prior to answering to the specific questions of the consultation paper, BNP Paribas would like to draw the Joint Committee's attention on the following issues:

# 1 Implementation timing

It is critical for manufacturers that all detailed rules are issued in their final form in sufficient time before the PRIIPs Regulation becomes applicable, as considerable IT based implementation will be required. Therefore substantially longer than 9 months will be required between publication of the final rules and the date the Regulation becomes applicable.

After having looked extensively at the Level-2 work done by the ESAs, we come to the conclusion that, due to the very technical nature of the underlying methodologies and calculations, there will not be enough time for market participants to fully implement the PRIIP KID by 31 December 2016.

The existing time constraints are also fully apparent in the work of the ESAs which, in spite of their considerable efforts, struggle to finalise their respective workloads before the end of the very ambitious deadlines. We notice this shortage of time in a number of conflicting and contradicting technical rules (e.g. on the calculation of risk), the introduction of completely new concepts at this late stage (e.g. arrival price for the calculation of transactions costs) and the general aim to include as many highly technical elements as possible in the draft RTS.
The latter is most apparent when comparing the current proposal to the existing UCITS KIID rules which provide a more general framework at Level-2, but subsequently identify technical details through Level-3 guidelines and Level-4 Q&As. It appears that the impending coming-into-force of the Regulation is the reason behind the ESAs not following this tried and tested model, as any provisions included into Level-3 guidelines would require further public consultation and thus risk derailing the finalisation of the overall framework.
Keeping these considerations in mind but being of the clear opinion that further consultations on the more technical aspects are needed, we request that certain provisions of the draft RTS be included in Level-3 or Level-4 measures. These include most of the annexes, but most specifically the risk calculation (calculations for market risk and credit risk) and cost calculation methodologies (i.e. table for standardised transaction costs).

# 2 Scope

In our opinion there still remains uncertainty regarding the scope for PRIIPs Key Information Documents. According to EU Regulation no. 1286/2014 a PRIIP is an investment product, and throughout the recitals and articles an investment with the purpose of obtaining a return based on a risk taken (speculation) seems to be in focus.

In Annex II, Part 1, 9(c) it is highlighted that all derivatives as defined in MiFID II are in the scope. But there is still no clarity as to whether derivatives are in the scope regardless:

- of whether they correspond to the definition of PRIIPs in the Regulation;
- of the underlying purpose – respectively speculation or hedging (of commercial and/or investment risk).

If derivatives used for hedging purposes are in the scope, the format and information contained in the KID will be misleading, as the purpose of the hedging strategy is to obtain exactly the opposite result of the derivative as a stand-alone investment.

## 2.1. Derivatives that do not correspond to the definition of PRIIPs in the Regulation

According to EU Regulation no. 1286/2014 (Article 4 ) a PRIIP "means an investment, including instruments issued by special purpose vehicles as defined in point (26) of Article 13 of Directive 2009/138/EC or securitization special purpose entities as defined in point (an) of Article 4(1) of the Directive 2011/61/EU of the European Parliament and of the Council ( 2 ), where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values or to the performance of one or more assets which are not directly purchased by the retail investor.

However in Annex II, Part 1, 9(c) of the ESA's joint consultation document it is highlighted that all derivatives as defined in MiFID II are in the scope.

This does not take into account that the characteristics of some derivatives do not correspond to those of PRIIPs as defined in the Regulation. Some derivatives represent an agreement between counterparties to exchange pre-determined cash flows and do not present any amount repayable subject to fluctuations.

They:

- do not involve exchange of cash flows based upon a floating reference rate or benchmark,
- are not leveraged instruments,
- do not contain optionalities.

Therefore, they should not be in the scope of the PRIIPS regulation. Those derivatives should only be subject to the MIFID II obligations in particular the obligation of price and cost disclosure.

## 2.2. Derivatives used for hedging purposes

Derivatives used for hedging purposes are often customized, and the consequences of expanding the scope of the KID to derivatives, used for hedging, do not seem to be analysed. If hedging is not out of the scope, there is a risk that small and medium sized companies will not have access to the necessary customized derivatives for hedging away risk.

Commercial hedging uses various derivatives, because banks provide this service, so the hedging client avoids the risk, when running a cross border business. If derivatives used for hedging purposes cannot be exempt from the regulation, the cost associated and the administrative complications will certainly be are too large, there is a risk of the banks only offering customized derivatives to very large corporate clients.

Small and medium sized corporations will then only have access to standardized derivatives leaving them in a situation where they will either have to take too large a hedging position (=a speculative position in the derivative for the surplus) or an insufficient hedging position leaving them with a residual of the commercial risk of running a cross border operation.

Also there is the risk of a concentration of issuers of derivatives, as only large banks can handle numerous customized derivatives. This could push further to a general concentration in the financial industry, as customers of smaller banks will have to consider whether they will only use banks offering the full range of transaction banking and hedging products. The risks described above will also apply where hedging is made of an investment position.

If small and medium sized corporations are forced to either under- or over-hedge. This may give rise to accounting issues (hedge positions) for the corporation. It has not been analysed further by the banking industry. When derivatives are used for hedging, there may often be an element of urgency as the commercial client which to mitigate the inherent risk of the commercial (or investment) arrangement instantly.

# 3 Alignment with MIFID II

MIFID II strongly interacts with PRIIPs at three levels:

- a target market may have to be displayed in the KID. Indeed, Article 8 (3) (c) (iii) refers to a Description of the type of retail investor and Article 4 of the draft RTS requires in the "What is this product" section to reflect the target market identified by the manufacturer. We assume that the target market referred to in PRIIPS is the target market which would be defined pursuant to relevant provisions of MiFID II. However this remains to be further clarified.

- the PRIIPS draft RTS specifies that when preparing performance scenarios, the manufacturer shall take due consideration to information used through the MiFID II the product governance process. Product governance process is a requirement under MIFID II. Since a one year delay

is likely to postpone the effective application of MiFID II it is likely that manufacturers may not have in place a process as robust as requested before January 2018.

- MIFID II sets an obligation to provide a full point of sale disclosure of costs notably when the firm is required to provide a KID under PRIIPs. Hence the cost disclosure format table under PRIIPs should be aligned with the format of MIFID2 Final TA from ESMA (2014-1569). So far those formats have not been harmonised.

We would therefore like to draw urgent attention to the fact that a decision to delay implementation of the MiFID II investor protection rules would have direct implications for PRIIPs and potentially result in manufacturers not having sufficient clarity on all content details for providing all required KIDs.

# 4 Insurance Products

Insurance sector is highly concerned by the inappropriateness of the PRIIPS regulation to multiple option products such as life insurance contracts including various investment options: (1) insurer's general fund, (2) insurer's Eurogrowth or growth fund, which (1) and (2) are both internal funds managed by the insurer, and (3) unit-linked investment products including units or shares of UCITS, structured products, units or shares in real estate funds or companies. There may be more than 800 unit-linked investment products offered under a life insurance or accumulation contract offered by insurers. In addition the customers may be offered the possibility to grant a mandate to an asset manager in order for the latter to select the assets in which his/her contract will be invested. Such mandates usually include two or three investment profiles (or more).

The insurer, as manufacturer, has a deep knowledge of its general fund and its Eurogrowth or growth fund, their cost and their risks. With respect to the other investment options (mandates proposed by asset managers other than the insurer) and unit-linked products, the insurer is not the manufacturer of those products and, should they be included in the KID referring to the insurance contract or the accumulation contract proposed by the insurer, the insurer would have to rely on information that it would obtained from other manufacturers and may incur liability for this. To this extent, it seems to us inappropriate and dangerous that the insurers include in their KID information relating to investment products that are not manufactured by them, as they may not have an appropriate knowledge of those products to provide reliable information in the relevant KID. We rather suggest that KID referring to life insurance and accumulation contracts may refer, with respect to unit-linked and mandates, to KIDs prepared by the manufacturers of those products.

Insurance product as funeral financing instrument:
In the French law context, life insurance contract also include contracts the redemption value of which should be allocated solely to the financing of funerals of the insured person. Those contracts have usually a low value and are not intended by the customers to be used as a saving instrument, but rather as a instrument financing funerals. It seems a bit weird to mention

market risk and credit risk and various scenarii for such products and therefore suggest that such contracts be excluded from the scope of PRIIPS regulation.

# 5 Performance Scenarios

The Consultation Paper requires the scenarios to be based on the "recommended holding period" and in addition, requires two other scenarios to be displayed for shorter “interim holding periods”.

For structured products, interim scenarios would be highly problematic because the mark to market at the “interim period” would have to be simulated at the date of the production of the KID, which is misleading because it would not be an indication of what the product can be worth in the future, yet many investors would understand it this way.

Instead, for products with fixed maturity dates such as structured products, we believe only one performance scenario should be required for that date. Interim dates in scenarios should only be used to illustrate cash flows (e.g. coupons or early redemption) of a structured product. Therefore the exemption to display interim scenarios currently only applicable in cases where products are considered to be illiquid according to Annex II part 5 paragraph 76, should be reworded to also include all products that have a fixed tenor such that only the scenario at the tenor should be displayed.

For products with no fixed maturity, the “recommended holding period” should be the one used in marketing brochures.

With respect to insurance products, at least for the French market, the holding period should be 8 years and 15 years.

# 6 Costs

## 6.1. Transactions costs

We are against the methodology prescribed by the ESAs to calculate potential transaction costs for a number of reasons where the PRIIP has been operating for more than three years:

- Apart for equities for which it may be possible to calculate the mid-market price (provided sufficient details are given to actually, in a level 3 Guidelines), for other assets data will either not be available or too burdensome to get.
- As the methodology proposed is simply a future estimate bases on three years of historic data, the outcome can never be accurate so there should be a cost-benefit trade-off in finding a suitable calculation methodology.

**Therefore we would like to suggest an alternative method:**

- Explicit or direct transactions costs should be used where possible ( e.g .broker fees, taxes , …)
- When explicit or direct transaction costs are not available (e.g. fixed income instruments) manufacturers would calculate standard transaction costs by using a standardized table provided by the ESAs for new PRIIPs, as no other information would be available. We favour using a standardised table to calculate transaction cost, which will allow for uniform calculation of transaction costs among all PRIIP manufacturers. This is especially important as the reliance on a standardised table will allow smaller PRIIP manufacturers to perform their transaction costs calculation without undue cost expenditures, which could put them at a competitive disadvantage.

## 6.2. Total costs

The 1st cost table is not clear that the Total Cost (sum of One-off, Recurring and Incidental Costs) divided by the Investment (e.g. EUR 1000) should equal the Reduction in Yield, which is an annualized number. This would be our understanding, but it is not stated clearly anywhere. Hence, for structured product, our intention is to compute the RIY as the Total Cost annualized by dividing the cumulative costs by the tenor. This would ensure numbers in the cost table add up, and comparability between structured products and UCITs funds.

For increased clarity, BNP Paribas recommends the holding period assumed for the presentation of costs to be the same than the one used for performance scenarios.

Given the length restriction that will apply for KIDs, we recommend to present only the first table instead of 2 tables, and incorporate the second table (which explains the nature of the cost) making a reference to the RTS themselves.

# 7 Risk indicator

## 7.1. Proposed methodologies for PRIIPS which fall into the categories III and IV :

7.1.1. With regards to structured products, the methodology to compute the MRM for structured product as a VaR Equivalent Volatility (Category III PRIIPs page.38 to 40 section 30 to 52) refers to a principal component analysis (PCA) for curves. The benefits of PCA are unclear. We believe manufacturer should be given the responsibility to compute the VaR of the PRIIP using audited internal models, and simulate product payoff using the Black & Scholes model calibrated with parameters derived from the historical sample, since this would give similar returns to a bootstrapping done over the same historical sample.

When credit itsef is the underlying (such as Credit Linked Notes), the Consultation Paper does not reflect the particular aspects of MRM. Section 60 simply prescribes to take the highest credit risk assessment for the CRM when credit exposure is at different layers, but it does not say how to compute the MRM. As of new, we suggest that the MRM for a credit linked note, would be the CRM that would have been assigned to the underlying entity of the credit linked note.

7.1.2. Regarding UCITS/AIFs, we disagree with the proposed methodologies for PRIIPS which fall into the categories III and IV :

For PRIIPS which fall into category III the "bootstrapping" approach is difficult to be justified. It seems that the industry standard "Historical simulation VaR" would produce the same results with much simpler calculations; a similar methodology already implemented for UCITS KIID structured funds (CESR/10-673) can be generalized in the PRIIPs context. The deviation from the industry's standards is difficult to be justified. We also consider that the calculations should be based on observables quantities and the methodology should be simple enough in to reduce the model risk and insure comparability of results .

In particular :

- Non observables quantities like expected dividends, borrow cost, (future) storage costs should not be used in the calculations as they cannot be projected in the future.
- Using the risk free rate (which by the way can be negative) as the expected return is justified in the risk neutral framework, but not in the historical one.

The category IV methodology is not explicit enough. It should be specified in a level 3 text, at least for PRIIPS invested in common products like real estate, private equities.

7.1.3. Regarding Insurance based-products

A VaR methodology is not the appropriate approach to evaluate the risk taken by customers when they invest in the general fund of the insurer for the following reasons:
(i) with respect to the general fund, an insurer has one data per year only, based on the minimum return rate guaranteed by the insurer (which may be null); such data obtained on a yearly basis may not be a sufficient data basis, in particular to use the Cornish Fisher approach;
(ii) in addition, the risk of loss for the customers is remote (unless the insurer falls bankrupt and the mitigating factors, being the prudential regime and the insurance guarantee schemes, fail to achieve their purpose) and the return of the general fund of an insurer, or the Eurogrowth fund, corresponds to a management decision of the insurer, taken in particular in light of the return of the assets in which the insurer has invested, the decisions taken by the customers (the selection of the assets in which they invest, their redemption requests) or the events affecting them (the death of the insured person) and the market and financial expectations of the insurer in the coming years. A VaR approach cannot reflect the management decisions taken by the insurer for the general fund or the Eurogrowth fund. As a result this would be misleading for consumers.

## 7.2. Methodologies for credit risk assessment

For AIFS or UCITS, we welcome the ESAs' statement on page 40 (para. 54 of Annex II to section 3) confirming that, in principle, credit risk shall not be assessed. We believe the cases outlined by the ESAs in relation to para.55 of Annex II to section 3 (on page 40, completed by explanatory text on page 76), in which credit risk is still meant to be considered for funds,

should be discarded, because all potential credit risk arising within a fund's portfolio impacts the fund's NAV and thus is already covered by its market risk. As a result, we think that for all calculations of the SRI, a fund's credit risk should always be considered as being CR1.

# 8 Grandfathering

There is no grandfathering provision in the regulation. Given the volume of PRIIPs outstanding, including the ones being offered in a continuous manner, a grandfathering period of 1 to 2 years should be granted to these products, so that their KIDs would need to be made available within a year after the regulation comes into effect.

# 9 Practical examples and technical rules missing

Consultation Paper does not provide technical rules specifically in the "What is this product" section, as well as some non-content related topics such as a clear updating requirement and example of what is continuously offered PRIIP vs a non-continuously offered PRIIP. BNP Paribas would like to stress that since there will be no further guidelines at a later point on level 3 or from national regulators, this means that practical implementation of the relevant requirements, especially "What is this product section", will then be left to interpretation of market participants.

We would welcome to see a KID template (in English) being introduced, for the most commonly traded structured products, such as reverse convertible, bonus certificates, or autocallable certificates. Also, such templates would serve the purpose of comparability and avoid the risk of national regulators providing recommendations at national level on how to draft KIDs.

**Question 1**
*Would you see merit in the ESAs clarifying further the criteria set out in Recital 18 mentioned above by way of guidelines?*

From a general point of view, we consider that further clarifications by way of guidelines would be welcomed for three reasons:

First, as that there are national divergences in the way structured products are regulated in the EU.

- The Spanish Ministry of Finance issued a regulation on the risk classification of financial products excluding PRIIPs, introducing a qualitative risk classification by way of a colour code, and specific comprehension alerts;
- The AMF (Autorité des Marchés Financiers) introduced a count on complexity mechanisms;
- The FSMA (the Belgian regulator) introduced in 2011 a Moratorium on complex products that gives its own definition of complex product and like in France introduced a count

on complexity mechanisms. There is also a regulation – currently put on hold – with a specific Belgian KID for all financial products, with specific risk indicators.

We would welcome a common approach on the use of the comprehension alert by the ESAs to avoid divergence in national practices. A PRIIP should have the same comprehension alert and same risk and cost indicator regardless of the EEA country in which it is offered.

Second, we disagree with the view that using a number of different mechanisms increases systematically the risk of misunderstanding on the part of the retail investor. What is at stake is the capacity of the investor to understand the risks he/she takes and the market scenario he/she anticipates. But it is not because a product uses derivatives or sophisticated mechanisms to deliver its performance that it has to be labelled as not simple and difficult to understand and be reserved to sophisticated investors: one should think in terms of intelligibility rather than in terms of complexity. Retail investors should not be discouraged to invest in innovative products, as long as they can perfectly understand the risks they take.
An approach based on mechanisms could be envisaged but only when a certain number of mechanisms is reached (as implemented by the AMF Position 2010-05). It should be noted however that such an approach is quite onerous in terms of defining what is or is not a mechanism and counting them for each new product.

Third, a clarification would be welcome in order to clearly identify the products in scope. We would like a confirmation that such criteria can be interpreted as complementary to those set out by ESMA Opinion on “MiFID practices for firms selling complex products” (7 February 2014) and by ESMA Guidelines on complex debt instruments and structured deposits (26 November 2015).

Regarding insurance-based products, we believe that it is of utmost importance that guidelines are established for, at least, each type of product.

**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?*

(i) We are of the opinion that these prescribed amounts should be amended as follows:
- EUR 1000 for structured products,
- EUR 10 000 for insurance products,
- EUR 100 for UCITS/AIFs.

(ii) Regarding structured products, whether the calculation is based on a default amount or the actual invested amount (or denomination, or notional amount) should not make any difference in the resulting %, but using the defaulting amount would probably enhance comparability. We are not opposed to use of another amount but like to still have the possibility to use the default amount even if the PRIIPs has a known minimum investment amount or denomination.

**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?*

- **With regard to both structured products and UCITS/AIFs,** Cornish Fisher expansion is an appropriate methodology. However, the wording in not always clear : (e.g. "daily equidistant prices". It seems that there are errors in formulae in the section 27, Section 10 mentions "daily" or "weekly" prices, but in the section 20 we see only "daily" prices. The section 20 should include cases where only weekly prices are available).

- **For structured products falling into category III,** we recommend to avoid using new methodologies, especially if they are not well-established market practices. We fear that not all market participants fully understand the bootstrapping. We observe that the results achieved by a bootstrapping using daily returns of a 5 years historical sample are similar to those from the well-established Black and Scholes model, using historical parameters estimated from the same 5 years historical sample. Therefore we fail to see the point of implementing the bootstrapping approach.

  The methodology chosen should produce similar result for a same payoff packaged under different wrapper, structured product or investment fund.

- **Only for UCITS/AIFs which fall into category III,** we do not recommend a bootstrapping approach.

Testing has proven that bootstrapping is unnecessary complex, worsening the computation time of the risk indicator, not well understood by all market participants, and it actually leads to similar results.
It seems that the industry standard "Historical simulation VaR" would produce the same results with much simpler calculations; a similar methodology already implemented for UCITS KIID structured funds (CESR/10-673) can be generalized in the PRIIPs context. Therefore, the deviation from the industry's standards is difficult to be justified. We also consider that the calculations should be based on observables quantities and the methodology should be simple enough in to reduce the model risk and insure comparability of results.

In particular:
- Non observables quantities like expected dividends, borrow cost, (future) storage costs should not be used in the calculations as they cannot be projected in the future,
- Using the risk free rate (which by the way can be negative) as the expected return is justified in the risk neutral framework, but not in the historical one.
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- **Regarding insurance-based products**, VaR approach is not appropriate to evaluate the risk of the general fund of the insurer or the Eurogrowth fund, where the invested amount is guaranteed by the insurer, on an everyday basis for the general fund or at the term of the guarantee period chosen by the customer, not being shorter than 8 years from the investment date, for the Eurogrowth fund.

As a matter of fact:

(i) with respect to the general fund only, an insurer has one data per year only , based on the minimum return rate guaranteed by the insurer (which may be null); such data obtained on a yearly basis may not be a sufficient data basis, in particular to use the Cornish Fisher approach;

(ii) in addition, the risk of loss for the customers is remote (unless the insurer falls bankrupt and the mitigating factors, being the prudential regime and the insurance guarantee schemes, fail to achieve their purpose) and the return of the general fund of an insurer, or the Eurogrowth fund, corresponds to a management decision of the insurer, taken in particular in light of the return of the assets in which the insurer has invested, the decisions taken by the customers (the selection of the assets in which they invest, their redemption requests) or the events affecting them (the death of the insured person) and the market and financial expectations of the insurer in the coming years. A VaR approach cannot reflect the management decisions taken by the insurer for the general fund or the Eurogrowth fund. As a result this would be misleading for consumers.

Should VaR approach be compulsory, the information delivered to the customers having invested within the framework of a life insurance contract or an accumulation contract would therefore be irrelevant.

**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.*

**With regard to structured products and UCITS/AIFs**, it is our view that a 5% level would be more appropriate as the results would be more differentiating for products with soft capital protection, having different barrier levels.

**Regarding insurance-based products**, VaR method is not appropriate for funds managed by the insurer (general fund and Eurogrowth fund) for the following reasons:

(i) with respect to the general fund only, an insurer has one data per year only , based on the minimum return rate guaranteed by the insurer (which may be null); such data obtained on a yearly basis may not be a sufficient data basis, in particular to use the Cornish Fisher approach;

(ii) in addition, the risk of loss for the customers is remote (unless the insurer falls bankrupt and the mitigating factors, being the prudential regime and the insurance guarantee schemes, fail to achieve their purpose) and the return of the general fund of an insurer, or the Eurogrowth fund, corresponds to a management decision of the insurer, taken in particular in light of the return of the assets in which the insurer has invested, the decisions taken by the customers (the selection of the assets in which they invest, their redemption requests) or the events affecting them (the death of the insured person) and the market and financial expectations of the insurer in the coming years. A VaR approach cannot reflect the management decisions taken by the insurer for the general fund or the Eurogrowth fund. As a result this would be misleading for consumers.

**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?*

- From a general point of view, we do not believe any statutory investor compensation or guarantee scheme should be taken into account.
  Government compensation scheme only guarantee EUR 100,000 or an equivalent amount, and it is not for each PRIIPs, but for each credit institution. Hence investors with more than EUR 100,000 in one PRIIP of one credit institution could be misled by a CRM risk class taking into account a compensation scheme.
  Furthermore, the existence of a compensation scheme is already specified in section "What happens if [the name of the PRIIP manufacturer] is unable to pay out?". We do not see the benefit of taking it into account in another section of the KID.

- Regarding insurance-based products, we are of the view that the existence of a compensation or guarantee scheme should be taken into account. Two mechanisms constitute reliable and powerful risk mitigating factors: (1) the very strict prudential regime applicable to insurance companies under Solvency II in order for them to control, manage and diversify their risks and ascertain sufficient solvency at any time, including under stressed scenarii, and (2) the insurance guarantee scheme established at national level, should an insurer face financial difficulties, it being understood that the aim pursued by that scheme is primarily to protect the investors and their savings. One may therefore consider that in light of those mitigating factors, the credit risk of an insurer is very low, if not immaterial. In addition, in the French market, the assets invested for the Eurogrowth or growth fund managed by the insurer shall be segregated from the other assets of the insurer and escape to all creditors' claims.

**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?*

We favour the option for manufacturer to voluntarily increase the disclosed SRI (could lead to defaulting to 7 for certain products hence avoiding actual calculation).

We do not have a view on unintended consequences.

**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?*

We disagree to adjust the CRM class for the tenor: this would be detrimental to the SRI computation and could have negative unintended consequences on the product offer as

manufacturers with poor credit rating would be incentived to design their products to benefit from a favourable credit assessment and show a better SRI.
The CMR class as proposed in the CP (based on ratings) are satisfactory.

Regarding insurance-based products, such adjustment of the credit risk for the tenor is not relevant for insurance-based products, that are, by nature, long term undertakings, depending on the life duration of the customers.

**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.*

We generally agree with the CRM scale and SRI matrix as they are defined in the CP. However, considering the MRM scale, we believe the most risky products (where the investors can loose more than the invested capital) should not fall within the same risk class and other PRIIPs but be assigned a specific MRM class of 8.

The alternative matrix presented in the questions section on the consultation paper (with only 5 credit risk classes) does not seem appropriate as it would not be discriminating enough between institutions rated "AAA" and "A" (all falling under CRM class 1).

For AIFS/UCITS, we welcome the ESAs' statement on page 40 (para. 54 of Annex II to section 3) confirming that, in principle, credit risk shall not be assessed. We believe the cases outlined by the ESAs in relation to para. 55 of Annex II to section 3 (on page 40, completed by explanatory text on page 76), in which credit risk is still meant to be considered for funds, should be discarded, because all potential credit risk arising within a fund's portfolio impacts the fund's NAV and thus is already covered by its market risk. As a result, we think that for all calculations of the SRI, a fund's credit risk should always be considered as being CR1.

With regard to insurance-based products, we consider that the scales of classes are arbitrary and are irrelevant for products depending on the life duration of their customers. Given the criteria currently contemplated, we understand that insurers would end up in CR3, which is in our view not a fair representation of the credit risk lying on an insurer, taking into account the Solvency II prudential regime and the insurance guarantee scheme implemented at national level.

**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?*

Generally, we do not have a view regarding PRIIPs that offer a capital protection during their whole lifespan and can be redeemed against their initial investment at any time over their life as BNP Paribas CIB does not offer such products.
If the capital protection is free from credit risk, we see no objection to assign MRM class 1 to such products.

Considering the 5 years tenor: in the low rate and low inflation environment, there are currently very few principal protected PRIIPs with less than 8 years tenor being issued.

Regarding insurance-based products, we agree that the general fund of the insurer and any other product that offer a capital guarantee during the whole lifespan and can be redeemed at any time for an amount at least equal to the amount initially invested on the product should be classified automatically in MRM1, irrespective of whether its tenor exceeds 5 years. We also believe that products offering a guarantee at an agreed term for at least 80% of the invested amount, such as the Eurogrowth fund or the growth fund of the insurer, should be classified above AIFs, UCITS and corporate bonds (not issued by insurers subject to Solvency II prudential regime).

**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?*

From a general point of view, we are not aware of any other circumstances mitigating the credit risk assessment. However, should any be identified, we believe it should only be taken into account if applicable to all type of PRIIPs to ensure an even playing field between products.

Regarding insurance-based products, we agree that it should be mitigated for insurance-based products given the mitigating factors applicable (Solvency II prudential regime and the insurance guarantee scheme applicable at national level).

**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?*

For UCITS/AIFS, the look-through approach should not generally apply in the case of PRIIPs investing in other PRIIPs or into other underlying instruments as suggested in para. 55 (d) of Annex II. The credit or counterparty risk involved with such investments should be considered part of the market risk as is the case for other investments in underlying assets and indeed, will be captured by the historical volatility data or performance simulations relevant for establishing the MRM category.

The look through approach may also be appropriate for certain unit-linked investments, but not in respect of the general fund or the Eurogrowth fund of the insurer. In light of the prudential

regime applicable to insurance and the insurance guarantee scheme, the risk of insolvency of the insurer is very remote.

**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?*

In our view, the risk indicator should relate only to the intrinsic risk of the PRIIP (measured in the currency used to issue the PRIIP). Therefore, the risk indicator should not 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.

If the investor needs to first enter a separate foreign exchange transaction prior to investing in a PRIIP in a different currency, the 2 transactions should be kept separate.

Regarding insurance-based products, we consider that currency risk should be taken into account for unit-linked products, where the underlying assets are denominated in a currency other than the currency of the insurance or accumulation contract. However, as the KID is pre-contractual information document and there is no reason for changing it, depending on the particular situation of a customer, we do not believe that it is necessary to take into account the currency risk for a customer that would subscribe a life insurance or accumulation contract in another European Union jurisdiction.

**Question 13**
*Are you of the opinion that the current Consultation Paper sufficiently addresses this issue? Do you 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?*

We believe it is made sufficiently clear that the value of a PRIIP could be significantly less during its life compared to the guaranteed value at maturity.
Article 9 of the draft RTS (how long should I hold it and can I take my money out early) already addresses this point).

**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.*

From a general point of view, performance scenarios should be presented net of all implicit costs to avoid any misunderstanding by the investor, implicit costs being defined as the sum of costs upon which the manufacturer has control, including the performance fee.

When possible to refer to a benchmark, the same benchmark should be used for all 3 scenarios. If performance fees are only charged when the PRIIP outperforms the benchmark, then performance fees should only be disclosed in the scenario where they occur (most likely not in the negative scenario).

For insurance-based products (general fund and Eurogrowth or growth fund managed by the insurer), it is important to emphasize that it is irrelevant as in the vast majority of products proposed by insurer, no performance fee is paid.

**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?*

We generally believe the table of Annex 1 is appropriate.

We disagree with graphs and prefer a table presentation. Only the table of Annex V - Appendix 1 should be required.

As explained in the general comment section, we suggest that, for products with fixed maturity dates, only one performance analysis should be required with reference to such maturity date.

Regarding insurance-based products, irrespective of whether the costs are presented in a table or as a graph, we believe it is important to provide for holding durations of at least 8 and 15 years for insurance-based products and that information on costs avoid any double-counting. Therefore we believe that disclosing direct costs would be more appropriate for the customers. Transparency on distribution costs will be achieved in accordance with other regulations, in particular MIFID II and IDD2.

**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?*

With regards to the asset classes listed, standard industry definitions are needed that correspond to the categories offered to practitioners by data providers such as Bloomberg. It would also be necessary to extend this table to other asset classes which PRIIPS invest in (Index, Tracker, ETf, deposit ,….) . A sub-categorisation of asset classes should be refined, at least in the long term, in order to better reflect the major drivers of transaction costs.

For example, possible criteria for further differentiation of bonds in terms of their trading costs could be the maturity term (since short-dated bonds generally imply different transaction costs than bonds with 30 or 50 years maturity) and the size of an order (in particular in relation to the overall trading volume of an instrument).

We are against the methodology prescribed by the ESAs to calculate potential transaction costs for a number of reasons where the PRIIP has been operating for more than three years:

- Apart for equities for which it may be possible to calculate the mid-market price (provided sufficient details are given to actually, in a level 3 Guidelines), for other assets data will either not be available or too burdensome to get.
- Even for equities it will be possible that a trade could incur negative transaction costs, if the market price at execution is lower than the mid-market price at the time of the order, in case the market collapse
- As the methodology proposed is simply a future estimate bases on three years of historic data, the outcome can never be accurate so there should be a cost-benefit trade-off in finding a suitable calculation methodology.

Therefore we would like to suggest an alternative method:

- Direct transactions costs should be used where possible ( e.g .broker fees, taxes , …)
- When direct transactions costs are not available (e.g. fixed income instruments) manufacturers would calculate standard transaction costs by using a standardised table provided by the ESAs for new PRIIPs, as no other information would be available. We favour using a standardised table to calculate transaction cost, which will allow for uniform calculation of transaction costs among all PRIIP manufacturers. This is especially important as the reliance on a standardised table will allow smaller PRIIP manufacturers to perform their transaction costs calculation without undue cost expenditures, which could put them at a competitive disadvantage.

**For insurance-based products**, we suggest to calculate direct costs, on the shorter recommended holding period (8 years), and a longer period (15 years), in respect of an invested amount that would be the same for all insurance-based products (e.g., EUR10,000).

**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)*

**With regards AIFS/UCITS** the table referred to in our answer to question 16 should be part of Level-3 guidelines rather than Level-2 RTS. The reason for this is that market spreads are a reflection of market volatility and do not remain constant for a period of three years. It is crucial that this table is maintained and updated on a constant basis by the ESAs to provide a relatively accurate description of current market spreads.

However for some instruments such OTC exotic options, OTC swaps, it may be difficult to get a standardized cost. So we recommend that PRIIPS providers may have the option to estimate the transaction costs figures for OTC products.

**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)?*

**Regarding UCITS/AIFs:** We generally agree that the values should reflect annualised amounts. Otherwise, the amount disclosed would appear to suggest that higher costs are incurred the longer a fund is held while in reality as the entry and exit charges are amortised over longer periods the annual cost decreases. The lack of annualised amounts may have a dissuasive effect on the investor. We believe the arithmetic average method would probably be easier to understand for a retail investor.

With regards to insurance-based products: to ensure comparability between PRIIPS, the values would be expressed as annualised amounts throughout the recommended holding period (at least 8 years and, for example, 15 years) and their calculation methods should be based on the guidelines to be set forth for at least each type of PRIIPS at national level.

**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?*

The suggested method is not appropriate to evaluate biometric risk premia. Generally, such premia should not be considered as a cost, they are the price to benefit from an insurance coverage. Aggregating those amounts with costs of saving products (such as a performance fee) may be misleading for the customers.

**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?*

We believe that biometric risk premia should be addressed separately, in the part of the KID describing widely the main characteristics of the insurance-based product (section "What is the product?"). In our opinion, it would be a non-sense to consider a reduction in yield for such premia.

**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?*

This point must be carefully considered also taking into account that MiFID II Delegated Acts require distributors to provide investors with information regarding the total aggregated costs of the products and the service both, as cash amount and as percentages.

The use of percentages is actually fine for table 2.
We do not expect any difficulties in calculating the monetary value for Table 1.
One important point is that for consistency reason the total cost divided by the invested amount and per year must be equal to the RIY (which is an annualized measure of cost). We have inserted an example detailing how we think Table 1 should be filled for a 5 years structured product with fair value equal to 98% and selling price of 100%.

We suggest adding that all costs in % in the second table are expressed per year so that their sums add up to the RIY.

| Cost Table 1 | | | | |
|---|---|---|---|---|
| Investment €1000 | If you cash in after 1 year | | If you cash in after 5 years | |
| One off cost | € | 20.00 | € | 20.00 |
| +Recurring Cost | € | - | € | - |
| +Incidental Cost | € | - | € | - |
| =Total Costs | € | 20.00 | € | 20.00 |
| RIY | 2% p.a. | | 0.4% p.a. | |

| Cost Table 2 | | |
|---|---|---|
| One-off Costs | Entry Costs per year | 0.40% |
| | Exit Costs per year | 0.00% |
| Recurring Costs | Portfolio Transaction per year | 0.00% |
| | Other Recurring Costs per year | 0.00% |
| Incidental Cost | Performance fee per year | 0.00% |

*we suggest to add that all costs in % in the second table are expressed per year so that their sum add up to the RIY

Regarding Insurance-based products, percentages would be easier to deal with for practical reasons but we agree that monetary values, based on annualised amounts over 8 or 15 years, would be more appropriate and easier to apprehend for customers. As a result, we agree with that proposal.

**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?*

Generally, we do not recommend a graph, the tables are clear as they are. A graphic presentation would be confusing and appropriate only when there is a cumulative effect on cost.

Regarding insurance-based products, we believe that a table showing the reduction in yield, setting out annualised amounts and avoiding any double-counting (hence referring to direct costs), calculated by reference to the guidelines to be established for at least each type of PRIIP at national level, would be clearer and less misleading for the customers.

**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 cost table above-mentioned includes all necessary information using a method that should be clear, understandable and not misleading for the customers, but should not showcase the variability of other cost elements. Referring to one scenario in a table or a graph showing the

costs would be misleading for the customers, as they may no longer understand the extra-information given to them.

**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?*

(i) From a general point of view, we believe that, given the length restriction that will apply for KIDs, the presentation of the prescribed cost items in the KID would better be restricted to only one table (instead of two, as proposed in the Consultation Paper).

In our view, the first table corresponds better to the customers' needs, and mixing up this information with those set out in table 2 may be confusing for the customers.

Regarding insurance-based products, the investment periods should be reasonable given the recommended holding period (at least 8 years, and 15 years may also be relevant).

(ii) As explained in Q23, we do not see the benefit of an additional graphic breakdown.

**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?*

Our understanding is that the RIY would be computed as a Total Cost annualized, defined broadly as the Total cost divided by the tenor of the product.

This would ensure numbers in the cost table add up, and comparability with UCITs funds.

We believe the calculation of the RIY (66 and 68) should be reworded and that example should be provided for structured products.

**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?*

From a general point of view, if the ESAs want to keep the 2 tables, then given the length restriction to 3 pages, we would favour a shorter presentation showing only the total cost.

If (and this is our preferred solution) the ESAs agree to have 2 tables merged into 1, we believe the breakdown of the 1st table is appropriate.

Regarding insurance-based products, we believe that the first table should detail entry, recurring and incidental costs. Otherwise it would be too difficult for the customers to understand the costs structure set forth in the contractual documentation of the insurance-based product. Expressing the total costs only would make it impossible for the customer to understand the link between the KID and the terms and conditions of the insurance contract subscribed by it.

**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.?*

We generally consider that for consistency and clarity, all types of costs in table 2 should be expressed on the same basis, i.e. an annualized percentage homogeneous to a RIY. This would ensure all cost item of Table 2 are adding up the RIY calculated in the first table.

Regarding UCITS, we recommend keeping the KID UCITS format.

**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 implementation of PRIIPS regulation, in particular with respect to unit-linked insurance contracts, will deeply change our relationship with other manufacturers of UCITs, structured products etc… This may have a deep impact on the product process, hence on the business of the financial sector. Therefore we need more time to establish the guidelines at national level (which is the condition sine qua non for achieving comparability between products) and review our relationships with other manufacturers, especially the UCITs' manufacturers. The success of this regulation will also depend on whether we will be able to display relevant and appropriate information that corresponds to the customers' needs for each type of PRIIP. We believe that other consumer testing, at national level, based on KIDs prepared by manufacturers of each type of PRIIP, would be very useful in order to ascertain the success of such ambitious but necessary reform. In case of failure, it would be very difficult to implement another instrument and this may have a deep impact on the business of certain manufacturers. This regulation is in our view too vital to be implemented within a tight calendar, without having regard to competition issues.