

**Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)**

**Deadline  
6 December 2018  
23:55 CET**

Name of Company:	Baillie Gifford & Co	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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<b>Reference</b>	<b>Comment</b>	
General Comments	<p>We welcome the opportunity to engage in this consultation. We consider this consultation as a preliminary step towards a more comprehensive review of the PRIIPs Regulation ('Regulation').</p> <p>The heart of any financial services transparency initiative should always be the protection of end customers – in this case, the consumers of products captured by the Regulation. With this in mind, our response to the questions that are part of this consultation revolve around the basic premise that information provided to consumers should always be <i>fair, clear and not misleading</i>.</p> <p>The intention of the Regulation is to protect consumers by increasing transparency and improving comparability between products. However, we strongly believe that certain information currently</p>	

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required to be included in the PRIIPs Key Information Document ('KID') has the potential to harm rather than protect consumers. Whilst we acknowledge that there is recognition amongst the ESAs of the issues that have arisen from the practical application of the detailed technical requirements included in the PRIIPs Commission Delegated Regulation 2017/563, we are disappointed that the proposals suggested in the consultation do not sufficiently go far in terms of completely addressing the following concerns: ***future returns scenarios that could be overstated, understated risks and unreliable transaction costs.***

Due to time constraints outlined in the consultation, the ESAs have decided to limit their review to performance scenarios. Whilst we agree that this issue is of utmost importance, other topics such as the simplistic way to calculate the Summary Risk Indicator ('SRI') and the use of 'slippage cost methodology' are as equally important and should also be considered for the reasons outlined below.

The method prescribed to calculate the level of risk is based on the historical share price volatility and does not take into consideration the capacity for loss to consumers from the investment. This simplistic way of calculating the SRI further exacerbates the already misleading information consumers can derive from the performance scenarios.

In previous FCA consultations, we have noted our disagreement with the 'slippage cost methodology' as the means to calculate implicit transaction costs as we do not believe that it gives an accurate picture of the true costs incurred. We would like to reiterate the same sentiment in this consultation. Apart from the fact that the use of this methodology can potentially lead to negative transaction costs, slippage costs cannot be relied on in estimating future costs as they are largely sensitive to trading styles and strategies, the particular benchmark used, and for some instruments (e.g. derivatives), the availability and reliability of intra-day prices.

Given these known issues, we believe it will be a **mistake to extend KIDs to UCITS funds without completing the review mandated by the Regulation and rectifying the issues that have the**

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	<p><b>potential to cause harm to consumers.</b> Therefore, we support the amendment in the cross-border distribution file to extend the UCITS exemption for another two years (end of 2021). Furthermore, we strongly urge the ESAs to include a proposal in their final report to broaden the scope of exemption to cover any non-UCITS funds that are currently not ‘marketed’ outside its home state. We consider this proposal to be in the interest of consumers as it temporarily minimises the use of KIDs without sacrificing the ‘spirit’ of the Regulation.</p>	
Q1	<p>Yes, we agree that information on past performance should be included in the KID. <b>Our preference is that, in line with the current UCITS KIID requirements, past performance becomes the standard disclosure and replaces the need for performance scenarios that we believe provide an overly positive outlook for returns and the clear potential to mislead consumers.</b> Whilst it is disappointing that time constraints are curtailing the opportunity to properly address the inclusion of performance scenarios, we agree that the disclosure of past performance alongside the existing performance scenarios would go part way to alleviating some of our concerns regarding existing KID disclosures. By allowing the disclosure of past performance, consumers will be provided useful context required in making an informed decision, with a graphical format over a 10 year horizon providing an investor with a better indication of the volatility of returns. As part of a more comprehensive review of the PRIIPS framework expected to be conducted in future years, <b>we would urge that serious consideration is given to having past performance replace the need for performance scenarios in KIDs.</b></p>	
Q2	<p>Structured UCITS KIIDs are currently not required to contain the past performance section. We believe that this should also be the case for structured CIS when producing KID.</p> <p>Whilst we welcome the proposed inclusion of past performance in KIDs, we believe that this does not really help the situation for new PRIIPs wherein KID producers are still expected to disclose future performance scenarios using an appropriate benchmark or index (i.e. representative fund) but are unable to disclose any past performance graph due to lack of price history. This means the potential harm due to inflated scenarios is not minimised.</p> <p>There was no mention in the consultation on how the past performance information will be included into the KID. Given the length of all the KIDs we are currently producing, we will struggle</p>	

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	to include the actual past performance table without exceeding the limit of a maximum of three sides of A4-sized paper.	
Q3	<p>Yes. Given that past performance information has been included in UCITS KIIDs for the last seven years, we believe replicating this is the most appropriate approach. Furthermore, there will be no need to perform testing on the presentation as consumers will already be familiar with it. However, for listed closed-ended funds like investment trusts, <b>we propose that past performance figures be based on the share price total return with dividends reinvested rather than net asset value.</b></p> <p>For a UCITS which does not yet have performance data for one complete calendar year, the UCITS KIID Regulation requires that a statement is included explaining that there is insufficient data to provide useful indication of past performance. In addition to this statement, we propose that KID producers are permitted to put the performance scenarios in context by (a) explaining the basis of the calculation (b) emphasizing that these are estimates and (c) including a note on potential volatility.</p>	
Q4	No. Article 19 (Use of ‘simulated’ data for past performance) of the Commission Regulation (EU) No 583/2010 (‘Article 19’) clearly states that a simulated past performance record for a period before data was available <b>shall only be permitted in limited circumstances provided its use is fair, clear and misleading.</b> We believe the inclusion of simulated past performance alongside performance scenarios that are themselves partly reflecting past performance is potentially misleading.	
Q5	We do not think that information on simulated past performance should be included in the KID. However, if ESAs take a different view, we suggest that the approach to be used, as well as the presentation, should be consistent with Article 19 and Article 44 (Fair, clear and not misleading information requirements) of the Commission Delegated Regulation 2017/565.	
Q6	Yes, we consider the amendments an improvement to the current performance scenario approach. However, we recommend that KID producers are allowed to include additional narrative to put the calculation in context and for the narrative not to be buried in ‘small print’ either by highlighting it in bold or including it in a separate section called <b>‘Important context in the calculation of performance scenarios’.</b>	

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<p>Q7</p>	<p>Our main concern is that the Regulation requires the industry to do something it has enduringly been discouraging consumers from doing – namely, estimate future returns based on past performance. We see real danger in doing this as the estimated future returns in the KID will be driven by market conditions prevailing in previous years which can lead to wholly unrealistic performance scenarios. We believe that neither amending the approach and presentation for future performance scenarios nor extending the historical period used to measure performance will be helpful as the fact remains that the performance numbers will continue to be misleading as they will still be based on historical performance. We do not support the use of risk-free rate of return to derive future performance scenario figures largely due to the fact that it provides meaningless information as under this approach all asset classes perform equally in future scenarios and as such there will be no difference between products. However, <b>we support using a model-based approach to future returns.</b> This is on the assumption that any change in the methodology will undergo a robust review process and thorough assessment including consumer testing before being implemented. Therefore, <b>we believe that any discussion on the methodology should be left as part of the planned wider review of the Regulation.</b></p>	
<p>Q8</p>	<p>In addition to changing the methodology to derive future performance figures, <b>we recommend that performance scenarios be limited to just the stress and favourable scenarios.</b> This is consistent with the requirement under Article 44 (Fair, clear and not misleading information requirements) of the Commission Delegated Regulation 2017/565 to show both negative and positive scenarios when disclosing future performance. Furthermore, when consumer testing was conducted in 2015, only three scenarios (favourable, non-favourable and neutral) were presented to the participants.</p>	
<p>Q9</p>	<p>Yes. However, we believe that the simplistic way of calculating the SRI further exacerbates the already misleading information consumers can derive from the performance scenarios. A less liquid PRIIP, a VCT for example, will appear to be at the lower end of the scale (below four – ‘low risk’) simply because its price moves infrequently when, in reality, a VCT is generally a high-risk investment because of the nature of its underlying investments. As such, <b>we recommend a methodology that incorporates an indication of capacity for loss from the investment be used.</b></p> <p>Furthermore, as per AIC Guidance on PRIIPs we suggest the following narrative be included to</p>	

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highlight that the SRI does not include all risks inherent in the product: *“The required summary risk indicator only reflects historic share price volatility of the shares. It excludes other risks inherent in the product and, therefore, does not show the full risk to the investor.”*

Q10

Our preference is that **short-term remedies are implemented to address the existing issues and also prevent the extension of the PRIIPs regime to UCITS funds** until a thorough and comprehensive review of the Regulation is completed. We believe it will be a **mistake to extend KIDs to UCITS funds without completing the review mandated by the Regulation and rectifying the issues that have the potential to cause harm to consumers.**

We are aware that an amendment has been proposed in the cross-border distribution file extending UCITS exemption from end of 2019 to end of 2021. We fully support this amendment. However, we cannot ignore the fact that whilst UCITS funds may be spared from producing KIDs, non-UCITS funds will have to continue to produce these knowing very well that there are fundamental issues that need to be addressed. **We strongly urge the ESAs to include a proposal in their final report to broaden the scope of exemption to cover any non-UCITS funds that are currently not ‘marketed’ outside its home state.** We believe this proposal is in the interest of investors as it temporarily minimises the use of KIDs without sacrificing the ‘spirit’ of the Regulation in terms of increased transparency particularly with respect to sales and distribution as non-UCITS funds marketed outside their home state will still continue to produce the document.

We do acknowledge the ESAs efforts to avoid a situation wherein consumers are provided with two KI(I)Ds once the UCITS exemption expires at the end of next year. However, given the number of articles in the UCITS KIID Regulation that need to be incorporated in the PRIIPs Delegated Regulation, we are concerned that there would not be any public consultation on the detailed text.

The consultation also assumes that professional investors may still be provided with a KIID. We question this assumption as we believe that it is highly unlikely that professional investors will require a key information document as they are more than capable of understanding complex information. In fact, from an ‘appropriateness’ perspective we are permitted to assume that a

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	<p><b>professional client has the necessary experience and knowledge in order to understand the risks involved in relation to the particular investment product.</b> Keeping the requirement to provide KIID to professional investors would just mean unwarranted resources being spent by management companies to produce two KI(I)Ds. To this end, we propose that this requirement is taken out once the UCITS exemption expires.</p>	
Q11	<p>In relation to option 1, one of the costs noted was that retail investors may unduly rely on past performance information and assume it will be replicated in the future. This is already the case with the existing methodology to derive future performance figures so will not represent as an additional cost.</p> <p>As to option 3, we do not agree that consumers may find the graphical presentation difficult to understand as this is not true in the case of a line graph as evidenced by the results of consumer testing. See excerpt below.</p> <p><i>When different ways of presenting performance information were considered, more complex graphical designs (showing a “funnel of doubt” or a “probability histogram”) did not perform as well as <b>simpler graphics which incorporated either a table or a line graph.</b></i></p> <p>For all options, the analysis of costs and benefits ignores the possibility of duplication of costs in terms of implementing the amendments which may be revised at some stage once a more comprehensive review has been completed. This may well be the case given that this ‘mini-review’ has not been specifically mandated by the European Commission (‘Commission’).</p>	
Q12	<p>We have confirmed with our PRIIPs KID producer that, if it is only a simple performance chart/table to be added in the KID, there would be no extra charge. If more work is required, costs will be shared between all their clients and themselves and they anticipate that this will be at a minimum cost to us.</p>	
Q13	<p>Any debate on the issues affecting the Regulation should have what is best for consumers at its centre. In its current state, we do not believe that certain information disclosed in KIDs meet the principles required when communicating to retail clients – <i>information should be fair, clear and not misleading.</i> Worse, it is leading to <b>unintended consequences that are potentially harmful to consumers.</b></p>	

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We welcome the ESA's initiative to introduce short-term remedies to address the most pressing issues surrounding PRIIPs KID disclosures. We appreciate the urgency of the matter due to time constraints, hence a targeted approach and shortened period of public consultation. However, we are disappointed that the proposals suggested do not sufficiently go far in terms of completely addressing the following concerns: ***future returns scenarios that could be overstated, understated risks and unreliable transaction costs.***

The Regulation mandates the Commission to review the practical application of the detailed rules by end of this year (31 December 2018). We have since heard that this review may be postponed for another year (31 December 2019). In light of the issues we have raised as part of our response to FCA's Call for Input, we strongly urge the ESAs to ensure that the Commission does not ignore its legal obligation to complete this review.