	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:	The Personal Investment Management and Financial Advice Association (PIMFA)	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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General Comments	PIMFA's member firms – consisting of wealth managers, financial advisers, execution-only brokers and investment platforms – play a very significant role in the distribution of PRIIPs to UK retail investors. In common with other sectors impacted by the PRIIPs regime, these firms have always supported its key objective (namely to enable consumers to compare the price, risk and performance features of different types of products and make informed investment decisions as a result) but have very serious reservations about whether KIDs produced under the current requirements are capable of producing disclosures that are clear, comprehensible and useful to investors. Furthermore, lack of clarity around both the scope of the regime and the application of its detailed provisions means that approaches to implementation have varied across the industry with the result that firms are now operating to widely inconsistent standards.	

Although we welcome the fact that the ESAs have recognised and sought to address a number of the most significant issues that currently bring the credibility of the KID into question, we believe that the ESAs' consultation exercise is misconceived, a "sticking plaster" that can neither hide nor address the fundamental flaws of the regime as a whole. Piecemeal amendments of the kind proposed run the risk of making matters worse than they already are, heightening the likelihood of individual investors being seriously misled and of industry being required to commit further resources to a regime that is clearly sub-optimal.

As we have recently made clear in our response to the FCA's Call for Input, PIMFA believes that the KID, as currently constructed, is providing investors with deeply flawed and potentially misleading information and that the PRIIP regime is in need of urgent and fundamental review. Given that the European Commission has made clear that it intends to defer the review provided for in Article 33(1) of Regulation 1286/2014, **PIMFA believes that the application of the PRIIPs regime should be suspended until such time as a full and through review is completed and a more informative, fit-for purpose regime - that both consumers and industry can have confidence in – can take its place.**

PIMFA considers that the vote earlier this week by the European Parliament's Economic and Monetary Affairs Committee – to extend UCITS' exemption from the PRIIPs regime by 2 years to 31 December 2021 and to set a new deadline of 31 December 2019 for the European Commission to complete its Article 33(1) review – paves the way for such an approach. While we recognise that the ECON vote only marks the beginning of a longer legislative process, it does appear to signal a wider recognition not only that the PRIIPs regime is significantly flawed but also that piecemeal amendments of the type proposed in this consultation are not the way forward.

Given the views set out above, PIMFA's response to the ESAs' consultation is largely focussed on outlining the difficulties that members have identified with the operation of the PRIIPs regime to date; our responses to the consultation questions should be read in light of these more general comments.

<u>Why the ESAs' "targeted review" is not the right approach</u>

PIMFA has identified three main areas of concern with the ESAs' "targeted review" approach – namely (1) the haste with which it is being pushed through; (2) the knock-on effect it may have on the European Commission's full review under Article 33(1) and (3) the fact that it paves the way for a potentially disastrous two-tier KID/KIID disclosure regime for UCITS from 1 January 2020. Specifically:

(1) As mentioned above, we believe that a piecemeal approach to addressing the major deficiencies of the PRIIPs regime is likely to be counterproductive. We also believe that a rushed review schedule – dictated by the timing of European Parliament elections rather than by the needs of the investors and financial services firms impacted by the regime – carries its own dangers in terms of the likely quality of the results of this exercise. Less than 6 weeks elapsed between the 1 October 2018 letter in which the ESAs announced their intention of undertaking a targeted review and the 8 November 2018 publication of this consultation – we consider it highly unlikely that legislative amendments cobbled together in such haste, without recourse to full consultation and industry/consumer testing, will do anything to improve a regime that took the best part of a decade and multiple rounds of consultation to reach its current far-from-perfect state. We are also concerned that, as well as being put to the time and expense of implementing significant amendments that they have had minimal opportunity to contribute to and critique in detail, firms will subsequently be required to either unpick such amendments or to implement yet others that re-tread the same ground.

(2) We note that the current consultation refers to "*a more comprehensive review of the PRIIPs framework*" being "*conducted <u>in the coming years</u>*". In contrast to the 31 December 2018 date set by Article 33(1) and the 31 December 2019 deadline more recently specified by the European Parliament, this timeframe sounds very open-ended, reflecting the European Commission's suggestion (in its 6 July 2018 letter to the ESAs) that "*the timing of the overall review will need to be also deferred*". We are concerned that the

ESAs' targeted review, by creating the illusion that the most problematic aspects of the regime have been addressed, will provide an excuse for a more fundamental review to effectively be put on hold. This would not be an acceptable outcome for the consumers who will continue to rely on sub-standard product disclosures or for the firms obliged to produce them and distribute them to clients in the knowledge that they are, in many important respects, either unclear or simply wrong.

(3) Again, as with (2) above, we are concerned that, by considering "*whether changes are needed to the PRIIPs Delegated Regulation specifically in view of the possible end of the exemption in Article 32 of the PRIIPs Regulation*", the ESAs' consultation may be seen to ease the pressure upon the co-legislators to address the ending of the UCITS exemption on 31 December 2019 as a matter of urgency. As we made clear in an addendum to our response to the FCA Call for Input, we do not believe that there are any circumstances in which retail investors should end up receiving a UCITS KIID and a PRIIPs KID, based on different requirements as to presentation and calculation, for the same product. The Commission's suggestion that guidance can in some way bridge the gaps between UCITS, PRIIPs and MiFID disclosures so as to ensure consumer understanding is nonsensical, as any firm that engages directly with retail investors would confirm.

Deficiencies of the PRIIPs regime

While the bulk of press comment on KIDs has focussed on the unreliable nature of the performance scenarios disclosed for certain types of products, the fact remains that there is no single element of the PRIIPs regime that can be said both to be completely clear in its intent and requirements and to be operating effectively. Notwithstanding the huge levels of resource that firms have expended in implementing the regime, it continues to bear comparison with Frankenstein's monster, a miscellany of ill-functioning parts that fail to add up to a coherent whole. If performance scenarios were the only part of the KID to be problematic, then a targeted review (albeit not one conducted as hastily as this one) might be the right response. However, when fairly much every element of the regime calls out for clarification and re-evaluation and when the on-going application of the regime seems likely to do many investors more harm than good, an immediate suspension of the regime combined with a wide-ranging and deep review is, we believe, the best course to pursue.

In its response to the FCA's Call for Input, PIMFA outlined its members' concerns about consumers being misled by the overly-optimistic performance indicators contained in many KIDs and about the possibility of firms themselves falling foul of their "fair, clear and not misleading" obligations as a result of providing customers with required documentation. Firms also commented on the KID being geared towards investors seeking a return on their investments and there consequently being little scope to adapt the document to fit the circumstances of client using derivatives for hedging purposes or clients for whom contracts are individually tailored to counter specific exposures. Beyond the issues publicly identified with KID performance scenarios, however, PIMFA also used the FCA's Call for Input to highlight a wide range of issues that undermine the practicability and reliability of the PRIIPs regime – these are summarised below:

- **Scope**. It has been extremely difficult for both providers and distributors to determine whether certain types of instruments (or, indeed, individual instruments within a particular category) are in scope. PIMFA has received many queries from its members about the PRIIP status of Real Estate Investment Trusts, AIM investing companies, corporate bonds, stapled/paired securities, subscription shares, royalty investment companies and offshore life insurance bonds. This lack of clarity has negative results for all market participants, circumscribing retail investor access to corporate bonds and requiring product manufacturers, data providers, platforms and advisers to engage in circuitous and wasteful debates about the PRIIP status of individual investments. At the same time, the widely different approaches that firms have adopted to classifying individual instruments and to making those instruments available to clients while their status is uncertain/under consideration, means that implementation of the PRIIPs regime across the market as a whole has been hugely inconsistent.

- **Third country products.** The PRIIPs regime is in urgent need of an equivalence mechanism that enables EU retail investors to access PRIIP-style products originating from non-EU jurisdictions. Firms have made clear to us that, with certain types of products no longer available to them (e.g. US mutual funds, US ETFs and offshore derivatives), investors are effectively being forced into investment options that may not be in their best interests, e.g. investing directly in overseas equities because non-EEA funds are not available or being unable to access the overseas derivative contracts needed to hedge non-EEA equity positions. In its July 2017 Communication (2017/C 218/02), the Commission stated that "*where retail investors within the territory of the Union decide to subscribe or purchase third country PRIIPs, ….. a person advising on, or selling, those PRIIPs must provide retail investors with a KID*". This is neither a practical nor an adequate solution to the difficulties that the PRIIP Regulation creates - as well as not having access to the data required to produce a KID, a retail distributor is unlikely to have the requisite knowledge/ expertise in the construction and operation of the product. Above all, no distributor can afford to assume the potential liabilities attendant upon producing what is effectively a "second-hand" KID for a product over which they have no control. In impeding retail investor access to all non-EU investment products, the PRIIPs regime is both detrimental to clients' best interests and anti-competitive.

- **Cost disclosure.** PIMFA members have expressed concern about the fact that implicit costs incorporated into KID cost disclosures are being calculated on different bases (i.e. using open/close prices instead of the true arrival price) and without manufacturers being required to specify the basis they are using – consequently, distributors have no confidence that, in looking across the transaction costs reported by different products, they are truly comparing like with like. This uncertainty also impacts firms' MiFID II costs and charges disclosures – firms have noted that, when providing an ex-ante figure for total costs and charges as required under MiFID II, negative transaction costs may result in total forecast costs being lower than will actually be the case. Furthermore, firms have experienced difficulties in explaining to retail clients (and, indeed, their advisers) what negative costs are and why, notwithstanding that they appear as a negative or a deduction, they make no difference to the overall amount a client pays.

- **Risk disclosure.** The existence of two similarly-named but differently-calculated risk indicators, both using the same 1-7 scale to cover hugely different populations of products, is undoubtedly leading some investors (specifically those who trade without advice) to make investment decisions based on erroneous comparisons of the relative risk ratings of certain PRIIPs vis-à-vis UCITS. This is borne out by research produced by the AIC which indicates that investment companies using the KID SRI are consistently shown as being lower risk than similarly-invested UCITS using the KIID SRRI, even though the former are generally regarded as being the higher risk of the two. Similarly, there are products whose SRI rating is at odds with wider market views or with the way in which they are used – the AIC highlights a large majority of VCTs achieving a SRI risk rating much lower than that accorded to most UCITS under the SRRI while firms in the PIMFA membership have suggested that the default risk-rating of 7 for derivatives is unhelpful when clients are being advised to use these to hedge other exposures.

- **KID distribution.** As we have made clear in previous correspondence with both the FCA and EIOPA, PIMFA believes that the exclusive focus of regulators on specifying requirements for KID presentation, content and calculation methodologies has resulted in distributors' queries about how and when KIDs should be delivered to clients in different circumstances being fairly much ignored. Queries brought to PIMFA's attention include how the Article 13(3) and 13(4) exemptions can be used; the meaning of "in good time before" in the context of on-line business; and the provision of KIDs when assets are transferred between accounts, when existing holdings are topped-up, when investment products are created for individual clients and when open offers provide clients with potential access to new products. Having received no regulatory assistance on these issues, firms have sought to resolve them individually, taking approaches that undoubtedly vary between different businesses but that seek to prioritise clients' interests and practicability.

	These issues are covered in greater detail in PIMFA's response to the FCA's Call for Input – the response and the accompanying letter focusing on the application of the PRIIP regime to UCITS can be found below: https://www.pimfa.co.uk/wp-content/uploads/2018/09/PRIIPs-CfI-FINAL-response.pdf https://www.pimfa.co.uk/wp-content/uploads/2018/10/PRIIPs-Addendum-to-CFI-response.pdf As we have made clear, we do not believe that the ESAs' consultative proposals constitute an adequate or appropriate response to the wholesale failings of the PRIIPs regime. Consequently, **our responses to the consultation questions should be understood in the context of our previous comments proposing that the regime be suspended, subject to thorough review/revision and then re-launched with a view to securing the confidence of both investors and industry.**	
Q1	We agree that information on the past performance of a product should be included in the KID where it is available, making necessary allowances for the expected lifespans of different product types. However, as per our general comments above, we believe that such amendments should be part of a wider review and not progressed on an interim basis.	
Q2	See Q4 below.	
Q3	For fund and other continuing/long-term investments, the KIID approach to past performance has many merits – as well as being familiar, simple and straightforward in terms of presentation, the KIID approach allows investors and their advisers to see the volatility of product performance over time and makes clear that the time an investment is made and the period for which an investment is held are significant factors in determining its overall performance.	
Q4	No. Simulations that rely on multiple assumptions and on the extrapolation of data derived from underlying investments are unlikely to produce information that is particularly relevant or helpful for investors. There must also be a danger that an unscrupulous manufacturer could finesse the structure/constituents of a product with a view to producing simulated past performance figures that effectively encourage consumer investment. Furthermore, experience shows that, regardless of all the warnings, caveats and assumptions with which any presentation of simulated past	

	performance might be surrounded, many (if not most) consumers will continue to rely on the numbers they are presented with when making an investment decision. If "*past performance is not a reliable indicator of future results*" (Delegated Regulation EU 2017/565, Article 44(4)(d)) when the data from which it is derived relates directly to the product in question, how much less reliable is past performance when it is conjured from data sourced from other, tangentially-relevant sources? Picking up on our earlier comments about the overly-hasty nature of the ESAs' targeted review and the potentially negative consequences of a process that does not allow for full consultation, we note the statement on page 14 of the consultation: "*For PRIIPs where actual past performance does not exist ….. the ESAs will consider the nature of any legislative provisions on the inclusion of information on past performance for these types of PRIIPs within the final RTS*." This seems to suggest that a simulated past performance methodology could be imposed on a wide range of PRIIPs via RTS that are to be endorsed by the Commission in January 2019 and finalised by mid-2019 without industry participants having any opportunity to provide detailed feedback on the construction, calculation or presentation of that methodology. Given that many of the current difficulties with KID performance scenarios derive from the failure of regulators to listen to the concerns previously expressed by industry about the content of Annexes IV and V of the PRIIPs RTS, this seems like an almost wilful blindness to the possibility of repeating past mistakes.	
Q5		
Q6	Although we do not support these amendments being made at the current time, we agree that the text proposed to replace elements [A] to [D] of Annex V is clearer, shorter and less repetitive than the existing text. Vis-à-vis the proposed heading for the performance scenarios table/s, we believe that the warning it conveys could be made both clearer and starker if the second sentence read: "These scenarios do <u>not</u> show actual returns – they are only an indication of the range of possible returns."	
Q7	Notwithstanding the deficiencies of the current KID performance scenarios, we are not in favour of significant amendments to the Annex IV methodologies being rushed through without full market consultation and testing – as we have previously commented, amendments to the	

	performance scenarios, as to all other problematic elements of the KID, should be managed in the context of a full review of the PRIIP Regulation. The ESAs have identified clear disadvantages to each of the options presented in section 4.1.6 – any decision to "try out" alternative calculation methods without being confident as to their ultimate impact risks not only making the current KID performance disclosures even less helpful for consumers but also putting product manufacturers to unnecessary work and cost in producing new KIDS for no good reason.	
Q8	In relation to the example showing the presentation of "Actual past performance" on page 17: • we query whether the statement "*Past performance is not a guide to future performance*" should be included. Past performance quite clearly is regarded as some sort of guide to future performance in the sense of its providing contextual information that can be taken into account in making an investment decision; if this were not the case, there would no reason to include it in the KID at all. Given this, we believe that the MiFID formulation (i.e. "*past performance is not a reliable indicator of future results*") that investment firms are required to use in all relevant information addressed to retail and professional client would be more appropriate. • the inclusion of actual past performance data (in combination with the extended narrative texts proposed for the SRI and performance fees) would add quite significantly to the overall content of the KID – given this, would the KID still be "*subject to an overall maximum of three sides of A4-sized paper when printed*"? As regards the provision of supplementary information, as covered in Section 4.1.7, we agree with the ESAs' concerns about such information potentially contradicting KID content and introducing inconsistencies into the way in which different products are presented. In a January 2018 statement, the FCA sought to address market concerns about the reliability of KID performance scenarios by suggesting that manufacturers could provide "*explanatory materials to put the calculation in context and to set out their concerns for investors to consider*" and that distributors could provide "*additional explanation as part of their communications with clients*". In their role as product distributors, PIMFA members have made the FCA aware of their objections to	

	providing "additional explanation", namely that they do not have sufficient knowledge to second guess manufacturer-produced data, they do not wish to introduce inconsistencies into the use of KIDs as product-comparison tools and they are not prepared to assume the liabilities involved in providing potentially inaccurate/incomplete information. More recently, members have confirmed that not only have they decided against providing any "additional explanation" of their own but they are also not aware of many manufacturers providing "explanatory materials" as suggested. In relation to Section 6 – setting out sample presentations of performance scenarios limited to just the stressed and favourable environments – the narrative text that follows both the table and graph formats appears to contradict itself. Having begun "*This graph presents the range of possible outcomes ….*", the text then states "*Actual future performance could be lower than described in the stressed environment or higher than described in the favourable environment*". While unknown variables such as holding period and future market performance mean that this is factually correct, consumers are unlikely to understand this nuance – the text as formulated is seemingly presenting the extremes of what is possible and then indicating that something on either side of those extremes may happen anyway – this is unlikely to result in consumers being confident about using KID information as a basis for making investment decisions. More generally, we do not agree with the suggested option of presenting future performance via two extreme scenarios – as well as making many products look far more speculative and volatile than they actually are, there is also the danger consumers will just assume that the most likely outcome is a return that falls right in the middle of the two extremes presented in the KID.	
Q9	No. For the reasons outlined in our general comments above, we do not believe that piecemeal amendments of the type identified in the ESAs' targeted review should be progressed in a bid to "shore up" a flawed regime. The items proposed in Section 4.2 should only be considered in the context of a full review of the PRIIPs Regulation.	
Q10	Article 33 of the PRIIPs Regulation outlines the nature/scope of the review to be undertaken by the European Commission – referring to the Article 32 UCITS transitional exemption and to the future relationship between the UCITS and PRIIPs provisions, it states: "*the review shall assess whether the transitional arrangements under Article 32 of this Regulation shall be prolonged, or*	

	whether, following the identification of any necessary adjustments, the provisions on key investor information in Directive 2009/65/EC might be replaced by or considered equivalent to the key investor information document under this Regulation." Similarly, the ESAs' November 2014 Discussion Paper states that the review will "*address any consequential measures in view of the end of this transitional period (i.e. amendments to UCITS, an extension of the transitional arrangements, or a decision to consider the UCITS KII requirements equivalent to the PRIIPs KID requirements)*." Nowhere is it suggested that – as per the current consultation - the PRIIPs Regulation itself will be amended to incorporate a large part of the UCITS Directive's requirements or that the application of those requirements will be extended to other non-UCITS PRIIPs. It appears to us that importing additional UCITS provisions into the PRIIP regime which are then applied to some PRIIPs but not others will introduce further inconsistencies and weaknesses into an already deficient regime and will undermine one of the KIDs main objectives, namely that investors can rely upon it when comparing investment products and coming to investment decisions. In short, we do not support broad swathes of the UCITS Directive being imported into the PRIIPs Regulation or the application of those provisions to non-UCITS products. Although the UCITS regime was developed to cater for a relatively homogenous range of open-ended collectives, it still provides for differentiation between various types of fund structures. Unlike UCITS, the PRIIPs regime covers an enormously wide universe of products, incorporating myriad structures, timeframes, constituent investments etc. Given this, it seems inconceivable that the possible extension of the PRIIPs regime to UCITS should in fact result in many/all PRIIPs being regulated as if they were UCITS. As well as aiming to effectively ring-fence the operation of the UCITS regime from the failings of the PRIIPs regime, the European Parliament's vote to extend the Article 32(1) exemption presumably also recognises that regulatory requirements for all products within the PRIIPs universe cannot be boiled down to what works for UCITS.	
Q11	In line with comments above, we fail to see how any meaningful assessment of potential costs and benefits can be made in the context of an exercise being managed at such headlong speed and without the mitigating discipline that might be provided by full industry consultation and in-	

	depth market/consumer testing. While the Section 5 CBA identifies at an extremely high level the sorts of costs that might arise from the ESAs' proposals, there is no recognition of the possibility that the proposed amendments may not have the desired effect and may have to be rescinded or finessed or may simply be a transitory staging post ahead of a full review identifying the need for more radical intervention. Every change to a regulatory structure as wide-ranging and complex as the PRIIPs regime results in myriad costs for firms – for this reason, repeated, piecemeal amendments that are in no way guaranteed to improve the existing regime should be avoided.	
Q12		
Q13		