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<tr><td></td><td>Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)</td><td>Deadline
6 December 2018
23:55 CET</td></tr>
<tr><td>Name of Company:</td><td colspan="2">German Association of Actuaries (Deutsche Aktuarvereinigung e. V., DAV)</td></tr>
<tr><td>Dis-closure of comments:</td><td>Please indicate if your comments should be treated as confidential:</td><td>Public</td></tr>
<tr><td></td><td colspan="2">Please follow the following instructions for filling in the template:
⇨ <u>Do not change the numbering</u> in the column “reference”; if you change numbering, your comment cannot be processed by our IT tool
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Our IT tool does not allow processing of any other formats.</td></tr>
<tr><td>Reference</td><td colspan="2">Comment</td></tr>
<tr><td>General Comments</td><td colspan="2">The German Association of Actuaries (Deutsche Aktuarvereinigung e. V., DAV) welcomes the ESAs’ intention to improve the PRIIPs KID and is very grateful for the opportunity to comment on currently proposed modifications. We generally appreciate that the ESAs are looking into methodological flaws of the PRIIPs RTS, especially concerning (among others)
• potentially overly optimistic performance scenarios,</td></tr>
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	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
	• lack of certain requirements for regular premium payments, • further specification of so-far unspecified or inappropriately specified requirements (e.g. the current mandatory narratives on the performance fees). As we understand, these targeted amendments are not to be mistaken with the general and presumably much wider review already foreseen by the PRIIPs Regulation which shall take place at a later stage. As the ESAs themselves acknowledge these targeted amendments are performed under a very challenging timeframe, which significantly limits the extent to which new approaches or methodologies can be developed. Taking this into account, we would advise not to integrate additional new and untested disclosures / methodologies (such as past performance or related simulated past performance) into the PRIIPs KID at this point in time. In our view any “quick fix” to solve the issue of overly optimistic performance scenarios should be thoroughly tested and consulted on. Otherwise it might potentially result in misleading results and hence not add much value to the customer’s perception of the KID. To overcome the issue of potentially overly optimistic performance scenarios several different approaches may be elaborated within the broader review, such as the use of a (somehow frequently calibrated) forward-looking stochastic model, or some related anchoring of performance scenarios of different asset classes according to their volatility/risk premium, or to the obtained market risk measure and many more. We acknowledge that any of these approaches might need further specification, therefore requiring thorough consultation and an impact assessment of potential results during the review process. Hence, in our view no quick fix regarding the performance scenarios should be initiated at this point in time (cf. remarks to question 7). Nevertheless, given the very short time frame, the ESAs should mainly focus on resolving those issues which currently lack definition in the RTS (such as requirements for the MRM calculation for regular premium payments) or yield an inappropriate disclosure (such as the current mandatory and potentially misleading narrative description of performance fees). In our view, it is sufficient to address these issues within Q&A for the time being. The big issues in our view (e.g. potentially overly optimistic performance scenarios, negative transaction costs) should be analysed within the broad review. On the contrary, some of the proposed modifications are in our view not necessary and may even lead to a less accurate and potentially misleading KID: Especially, the introduction of past performance, the discussed use of risk-free scenarios, the proposed removal of aligning the disclosure of charges to the moderate performance scenario all seem to be inappropriate and potentially misleading and should therefore not be implemented (cf. remarks to questions 2 and 8).	
Q1	**Do you agree that information on past performance should be included in the KID where it is available?** As already mentioned in the general comments, we do not consider it appropriate to include past performance scenarios in the PRIIPs KID.	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
	Article 33 of Regulation 1286/2014 provides for a review. The postponement of the first application to 1.1.2018 did unfortunately not lead to a corresponding adjustment of the review date. However, the review should still be well prepared and should be preceded by consumer testing and consultations with experts and stakeholders. The present consultation does not fulfil this legal mandate. We are convinced that past performance as additional information does not solve any of the problems outlined by the ESAs. In our view, it results in misleading information in the KIDs. This has also been stated in a previous discussion paper by the ESAs, cf. JC/DP/2014/02. This statement is correct for all product categories and applies in particular to long-term insurance based investment products. The information on past performance would be misleading as: • Past performance does not make any statements about the future. A corresponding disclaimer is therefore always included for past performance. • Past performance supports a procyclical behaviour of retail investors. • Past performance systematically overestimates the return (keyword: survivorship bias). • Past performance does not allow any conclusions to be drawn about the quality of the manager of the investment, as there is no benchmark. • Past performance with a 10-year history does not cover all economic cycles (e.g. not the 2008 financial crisis). • The presentation of past performance and the results of methods for products in categories 2 and 3 reinforce the problems already identified by the ESAs for these methods. • If the information on past performance were included, 3 pages would not be sufficient for the KID.	
Q2	**Are there challenges to include past performance information for certain types of PRIIPs?** We recommend conducting a detailed review later on, based on a proper consumer testing and consultations with expert groups as well as other stakeholders. The introduction of an intermediate solution is not advisable. We do not consider past performance scenarios to be appropriate for investment based insurance products (IBIPs) for the following reasons: • Many IBIPs do not have market values. Thus the UCITS NAV methodology is not applicable. Alternative definitions of past performance would have to be developed found. Currently no meaningful definition is available that would give meaningful results for all IBIPs. IBIPs differ significantly between Member States. It is unclear whether a unified approach for past performance can be developed which allows results to be comparable.	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
	• The ESAs themselves acknowledge that there is no existing definition for all products. In the consultation a simulated past performance is mentioned. However there is no definition given in the consultation. It is rather unclear what is being envisioned here. The DAV is not aware of any methodology for simulating past performance which takes a holistic view at long-term insurance products which often include profit participation and biometric components. Therefore, we are very skeptical that a workable solution for past performance exists for all IBIPs. • Also the presentation of UCITS past performance as a collection of ten years of yearly returns does not fit the characteristic of many IBIPs which are long-term products with holding periods much longer. This presentation would suggest to consumers that the product was meant to be traded on a yearly basis. • IBIPs often have very long contract terms but due to necessary changes (e.g. regulatory changes, technical interest rate, costs changes) a new product generation has to be introduced every couple of years. Thus, the currently sold products do not have a sufficient track record to take a holistic view of the products past performance. • IBIPs often insure biometric risks. First of all biometric risk cannot be observed in past performance. Second of all the different tables for mortality, disability and longevity have to be updated regularly also resulting in new product generations. The current products were there-fore not available in the exact same form in the past. Therefore, it is not possible to properly include biometric features thereby precluding a holistic approach. For products with profit participation the biometric risks are covered by the same with-profit fund as the rest of the prod-uct. • Neither guarantees nor death benefits hold any value in the past as no uncertainty remains. One of the main features of insurance is pro-tection against uncertainties which would be completely ignored with a past performance approach. • In several Member States IBIPs are based on individual contracts. Past performance therefore varies between contracts with different agreed upon holding periods. Furthermore it might depend on which year of the contract you are in as costs are often not distributed evenly over the holding period. For this common type of contract only rough averages could be given.	
Q3	**Do you agree that it is appropriate for this information on past performance to be based on the approach currently used in the KII? If not, please explain your reasons and if an alternative presentation would be more appropriate and for which types of PRIIPs?** We recommend conducting a detailed review later on, based on a proper consumer testing and consultations with expert groups as well as other stakeholders. The introduction of an intermediate solution is not advisable. Currently in the UCITS KII a yearly bar chart covering the performance over the last 10 years is used. This type of presentation contradicts the character of an insurance-based investment product (IBIP). The majority of IBIPs are long-term products and, therefore, it is important for consum-ers to use a holistic approach that includes the effect of long-term saving as well as biometric protection. There should be a strong focus on the cumulated gain contributing to the long-term yield, for example with regard to retirement questions and the occurrence of the insured event. Less relevant for consumers is the yield produced last year.	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
Q4	**Do you think that information on simulated past performance should be included in the KID where actual past performance is not available? If not, please explain your reasons.** We recommend conducting a detailed review later on, based on a proper consumer testing and consultations with expert groups as well as other stakeholders. The introduction of an intermediate solution is not advisable. We fully agree with the ESAs that there is no existing definition of past performance for all types of PRIIPs. Currently no meaningful definition of past performance is available that would give useable results for all investment based insurance products (IBIPs). IBIPs differ significantly between Member States. It is unclear whether a unified approach for past performance can be found which allows results to be comparable. We do not consider simulated past performance to be appropriate for investment based insurance products (IBIPs) for the following reasons: • There is no definition of simulated past performance given in the consultation. It is rather unclear what is being envisioned here. The DAV is not aware of any methodology for simulating past performance which takes a holistic view on long-term insurance products which often include profit participation and biometric components. Therefore we are very skeptical that a workable solution for past performance exists for all IBIPs. • Also the presentation of UCITS past performance as a collection of ten years of yearly returns does not fit the characteristic of many IBIPs which are long-term products with holding periods much longer. This presentation would suggest to consumers that the product was meant to be traded on a yearly basis. • IBIPs often have very long contract terms but due to necessary changes (e.g. regulatory changes, technical interest rate, costs changes) a new product generation has to be introduced every couple of years. Thus the currently sold products do not have a sufficient track record to take a holistic view of the products past performance. • IBIPs often insure biometric risks. First of all biometric risk cannot be seen in past performance. Second of all the different tables for mortality, disability and longevity have to be updated regularly also resulting in new product generations. The current products were therefore not available in the exact same form in the past. Therefore it is not possible to properly include biometric features thereby precluding a holistic approach. For products with profit participation the biometric risks are covered by the same with-profit fund as the rest of the product • Neither guarantees nor death benefits hold any value in the past as no uncertainty remains. One of the main features of insurance is protection against risk which would be completely ignored with a past performance approach. • In several Member States IBIPs are based on individual contracts. Past performance therefore varies between contracts with different agreed upon holding periods. Furthermore it might depend on which year of the contract you are in as costs are often not distributed evenly over the holding period. For this common type of contract only rough averages could be given.	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
Q5	**If you think that information on simulated past performance should be included in the KID, what approach do you think should be used to simulate the past performance, and how should this be presented in the KID?** We recommend conducting a detailed review later on, based on a proper consumer testing and consultations with expert groups as well as other stakeholders. The introduction of an intermediate solution is not advisable. In our view, consumers do not benefit from simulated past performance, for the reasons set out in the answers to questions 2 - 4.	
Q6	**Do you consider these amendments to the narrative explanations to be an improvement on the current performance scenario approach?** The current future performance scenarios intend to help the consumers to compare products and understand how their outcomes might develop in the future. This is done by showing a range of outcomes. The real outcome in the future may be somewhere within the range or even better or worse. The scenarios shall not give undue certainty to these outcomes. It is very important that the narratives enable consumers to understand the restrictions and the right interpretation of the underlying methodologies. We are convinced that additional information (“Market developments in the future cannot be accurately predicted. These….”) would be helpful for consumers. We prefer that possible amendments for the future scenarios should be implemented within a detailed review later on, based on a consumer testing to assess the impact of the improvements.	
Q7	**Do you have any comments on the analysis set out in this Section of other possible options to improve the future performance scenarios?** **Future performance scenarios anchored in the risk-free rate of return** We acknowledge that the current specification of performance scenarios for products of category 2 and 3 may yield potentially overoptimistic projected performance scenarios due to the reliance on the observed returns of the past five years. Therefore, to resolve this issue, one approach being suggested by the ESAs is to anchor the projected returns to the risk-free rate instead of the average return observed during the last five years return. This approach then essentially corresponds to a “risk-neutral” projection of the underlying assets. From an economic point of view risk-neutral projections are only meaningful for assessing the (market-consistent) price of an underlying security/derivative by calculating its price by means of expected discounted cash flows and should therefore not be applied when “real-world” percentiles of potential returns shall be esti-	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
	mated. If all future returns were anchored to the risk-free rate, then a money market investment would probably yield the most attractive investment option from a retail investor's point of view, since different asset classes would only come with a higher volatility but no (potentially existing) risk premium would be credited for. Hence, we would strongly advise that performance scenarios should not be anchored to the risk-free rate, since they would lack economic meaning and yield misleading information to the retail investor. However, some anchoring approach might still be feasible. Based on e.g. a forward-looking (and appropriately calibrated) modelling approach, risk premiums for different asset classes might be obtained. Then, according these "asset class specific" risk premiums the volatility of each fund within the asset class could be used to "scale" the specific fund's risk premium accordingly. It could also be discussed if it were possible to link the assumptions for performance scenarios to the obtained market risk measure for different asset classes by anchoring them appropriately. **Amended approach and presentation for future performance scenarios to highlight the range of outcomes** In our view, reducing the number of performance scenarios from four to two and hence only disclosing a range of potential outcomes may be perceived as the total range of possible outcomes. A range might indicate that (although the related narrative explanations are possibly additionally amended) the future benefit payments will for sure lie within the disclosed range. Hence, if the range is too narrow, this may result in consumer detriment in the future, if actual outcomes were not in the previously disclosed range. Further, if the disclosed range is in contrast too wide (note the proposal is to disclose the stress and the optimal scenario) the information provided might be of very little additional value to the customer. In addition, due to the different underlying methodologies of deriving the stress and performance scenarios, there are examples where the stress scenario yields higher returns than the other performance scenarios and hence the proposed range is not meaningful. Therefore, we would stick with the current disclosure of four different performance scenarios and not reduce them to two and rather amend the actual derivation of the performance scenarios (within the wider review). **Extend the historical period used to measure performance** In our view, the extension of the past time frame for deriving the performance scenarios generally bears the same flaws as the current specification. Hence, the currently observed overly optimistic scenarios could (as the ESAs also acknowledge) even be pronounced by extending the historical period for estimating the performance scenarios as market cycles can be even longer than ten years. In our view, the general methodology to assess the performance scenarios of category 2 and 3 should be amended instead of "just" extending the observation period.	
Q8	**Do you have any views on how the presentation of the performance scenarios could otherwise be improved?**	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	Deadline 6 December 2018 23:55 CET
	As already indicated, we think that the actual derivation of future performance scenarios for products of category 2 and 3 should be generally revised taking the current issues into account. This revision should however be thoroughly tested and consulted on and can hence only be subject to the broader review already set out in the PRIIP directive. An approach to derive the performance scenarios could be based on a forward-looking stochastic model (for different asset classes) which would be regularly calibrated by some external party (e.g. the ESAs) to account for current market developments on the one hand, and on the other ensuring "consistent" and generally stable/smooth results of projected returns over the lifetime of a PRIIP.	
Q9	**Do you agree with the proposals described in this section?** **Market risk measure (MRM) calculation for regular investment or premium PRIIPs** We appreciate that the ESAs specify the currently non-specified treatment of regular premium payments when the MRM is derived in detail. Further, in our view, regular premium payment flows can only be appropriately treated applying some approach based on simulations. Therefore, the proposed idea for products of category 2 is consistent to a projection of a single premium payment and should hence (neglecting the general issues of the Cornish-Fisher approach itself) be applied. We expect that similar amendments will also be made for deriving the performance scenarios when regular premium products are considered. However, we believe that the approach taken should be described in more detail so that every step of the procedure is clear to the manufacturers. In the broader review to come, the ESAs should further assess if the currently proposed methodology to derive the VEV from the simulated Value-at-Risk is actually appropriate and fits to the qualitative requirements on VEV for regular premium payments or if it might need further modification. **Growth assumption for the reduction in yield (RIY) calculation** We agree that for some PRIIPs with negative or very low moderate performance scenarios the disclosure of charges may be challenging or problematic. However, removing the link of potential future performances to potential future costs by arbitrarily setting the assumed return for the disclosure of charges to 3% will puzzle the customer when he tries to assess the costs and benefits of the product. The RIY and the total amount of charges is dependent on the yield assumed for its calculation, thus the yield used for the calculation should be consistent to the rest of the KID. This issue particularly materializes when the assumptions for potential benefits massively differ from those when costs are disclosed. A mandatory requirement to derive the cost disclosure for a return of 3% may also set the incentive to implement charging structures that yield minimal (or even no) costs when the underlying returns were exactly 3% and heavily differ for different (real-life) returns. In our view, the reason for potentially puzzling cost disclosures when low or negative yielding moderate performance scenarios are considered, can primarily be found in the specification of the performance scenarios itself and not the related disclosure of charges.	

	Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)	**Deadline 6 December 2018 23:55 CET**
	Therefore, in our view the current alignment of cost disclosure and the moderate performance scenario shall be still maintained in the updated version of the RTS.	
Q10		
Q11		
Q12	**Are you able to provide information on the costs of including information on past performance for different types of PRIIPs?** For products which include biometric risk protection (such as insurance-based investment products) past performance does not exist. For consumers it will be very hard to understand the concept of simulated past performance and, therefore, the added value will be very small. It is not at all sure, whether the added value of simulated past performance is big enough to justify that it is included in the KID (which should only provide key information to consumers). We recommend conducting a detailed review later on and including improvements to the current approach for generating future performance scenarios in this detailed review. Changing the performance scenarios too often might lead to a loss of confidence among consumers.	
Q13		