European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

EACB Comments on

Workshop document:
Packaged Retail Investment Products
Issues for discussion

16 November 2009

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General remarks

- EACB is in principal in favour of the Commission approach expressed in the discussion paper. Especially welcome is the acknowledgment of the European Commission that no one size fits all approach will be used for the key investor information although the Key Investor Document (KID) for UCITS naturally offers elements to be used.

- The key investor information as well as the KID will be only one building block within an series of measures to improve the information base for the retail investment decision, like prospectuses, information brochures and, last but not least, financial education.

- EACB supports the inclusion of packaged retail products with mid- to long-term period, high investment risk with regard to the invested capital and to performance. On scope, some adjustment to capture the relevant products is needed.

- EACB shares the view that MiFID should be the benchmark on how to treat the PRIPs products and that no enhancement of MiFID rules is necessary. In addition it notes that CESR is currently in the process of clarifying several very important elements of MiFID (such as the "complex-non complex" distinction and the definition of "advice"). As a matter of example, in the recently published document by CESR (3 November 2009), the following can be read:

  "*Do the appropriateness requirements apply to deposits, mortgages or life insurance products?*

  These questions have been addressed by the European Commission in its MiFID Q&A database (notably Q&A 118 and 203). In summary, the answer is "no" to all of the above, since these are not MiFID financial instruments listed in Section C to Annex 1 of the MiFID Level 1 Directive. The exception to this is that the Commission regards a deposit with an embedded derivative that has the potential of reducing the initial capital invested as a financial instrument under MiFID."

  And also:

  "*All investments in UCITS are non-complex instruments by definition, for the purposes of the appropriateness requirements, regardless of the underlying instruments in which the UCITS invest. Nothing in MiFID Art. 19 (6) requires a person to look through to the underlying investmetns of the UCITS for these purposes*"

- EACB agrees in general with the Commission proposal acknowledging that the packaging of products constitutes for investors an additional layer of complexity which is not well understood. EACB supports a practical approach towards this topic: e.g. products with a capital guarantee should be subject to a different treatment within the scope of PRIPs, and deposits should be out of the scope of the PRIPs rules altogether. This is justified because capital guaranteed bank deposits show a distinct nature in terms of client protection, due to the fact that their guarantee is not only given by the issuer, but also by the respective state within the Deposit Protection Schemes.

It would be important to focus on the perspective of investors and whether they understand the product. It might be necessary to distinguish between "packaged" and "wrapped" products from this perspective. Because even if the structure of some wrapped products might be complex, the underlying risk/return profile of "wrapped" products is easy to understand for investors and therefore do not deserve to be included. A "wrapped" product could be defined as an investment product that, although presented to the client "wrapped", simply offers him or her access to an underlying investment whose risk is well understood by retail clients and in which a retail client could in fact easily invest directly (i.e. funds or bonds linked to a well-known equity or fixed-rate index, or to a security traded in a regulated and available-for-retail-investors market).

- EACB welcomes the responsibility of the "manufacturer" of the product because of the detailed knowledge of the product on his or her side and the need for a clear and practicable solution. In any case, close cooperation with the distributor side will be needed which should be left to the distribution arrangements between both sides.

- EACB does not favour a renewed debate on open architecture connected to the PRIPs project as it seems to be the case in the discussion paper in question 17.

- The summary of the prospectus should not take elements of the KID, because the prospectus is an instrument of disclosure for the issuer whereas the KID focuses on product information at the point of sale and therefore has a meaning which is different from the highly complex prospectus and its summary (see the proposal COM(2009) 491 final for a directive of the European Parliament and of the Council amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation oftransparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market).

- On cost disclosure, the KID should show distribution costs, not manufacturing costs. MiFID as the benchmark for cost disclosure does not need any revision or refinement in this regard.

Answers to the different questions

1. **Are the above mentioned criteria and the related approach able to capture the relevant market of PRIPs across jurisdictions? Are they able to achieve the identified objectives? Are there other elements to be considered?**

EACB supports the exclusion of the scope of PRIPs of bank deposits, on the following grounds:

EACB certainly supports the exclusion of saving deposits because they represent neither risky nor packaged or wrapped products and are covered by compensation schemes. This legitimates the exclusion of saving deposits although the outcome of the investment in saving products is not known beforehand (p. 3 third bullet point from above) because of the variable investment periods as well as volumes, the dependency of the interest rate on the market rate which is the criterion for defining saving products in contrast to term deposits with fixed rates, fixed volumes and investment periods.

The same goes for saving deposits designed for retirement provision with an often quite long investment horizon and dependency on capital market indices, e. g. EURIBOR.

Term deposits are short-term oriented, covered by compensation schemes and very transparent for investors. Therefore they should be out of scope even in case of structured elements affecting the payout profile.

EACB agrees in general with the Commission proposal acknowledging that the packaging of products constitutes for investors an additional layer of complexity which is not well understood. EACB supports a practical approach towards this project: e.g., products with a capital guarantee should be subject to a different treatment within the scope of PRIPs, and Deposits should be out of the scope of the PRIPs rules altogether as it will be argued later. This is justified because capital guaranteed bank deposits show a distinct nature in terms of client protection, due to the fact that their guarantee is not only given by the issuer, but also by the respective state, within the deposit protection schemes.It would be important to focus on the perspective of investors and whether they understand the product. It might be necessary to distinguish between "packaged" and "wrapped" products from this perspective. Because even if the structure of some wrapped products might be complex, the underlying risk/return profile of “wrapped” products is easy to understand for investors and therefore do not deserve to be included. A “wrapped” product could be defined as an investment product that, although presented to the client “wrapped”, simply offers him or her access to an underlying investment whose risk is well understood by retail clients and in which a retail client could in fact easily invest directly (i.e. funds or bonds linked to a well-known equity or fixed-rate index, or to a security traded in a regulated and available-for-retail-investors market).

Covered bonds are no wrapped products and should be out like plain vanilla bonds.

2. **Are there other products which should be included in the PRIPs work, and how might these impact on the approach to scope outlined above?**

No.

3. **How should we handle non unit-linked/index-linked "traditional life insurance"/life insurance 'with profits' contracts, which in some jurisdictions are sold as investment / accumulation products?**

n/a

4. **How should we handle products which sit on the boundary of the PRIPs market but are also sold in some jurisdictions as retail investments e.g. "pure derivatives"?**

In case of “pure” derivatives in retail business no wrappage or package is to be found. In retail business, equity options and bond futures are preferred and short-term oriented. Therefore MiFID rules should suffice here.
In the case of listed derivatives a high degree of transparency is ensured. OTC derivatives are rather seldom used in retail business and if they are, they are used to hedge risks. Products like interest rate swaps and interest caps prevail with no need for a special regulation, as they reduce or limit the retail client´s exposure to interest-rate risk.

5. **What is your view on how "pensions" and annuities should be treated? Should they be included? Can they effectively be excluded? Are there certain types/categories of pension products which should be included?**

n/a

6. **Would you agree that we have identified the right principles which should govern a common framework for all PRIPs? Are there other elements to be considered?**

We believe that the complexity inherent to the “structure” justifies the PRIPs regime, but that other concepts have to be taken into account when looking for a practical approach that really adapts its provisions to the problems faced by investors in their day-to-day investment decisions. In particular, we argue for taking also into account the concepts of [“packaged”-“wrapped”] and [“risk” (in the sense of “capital guaranteed” or not, and in the sense of the coverage by a deposit guarantee scheme)].

We have doubts about the following formulation in the discussion paper: “KID to be provided to retail clients in good time before any commitment is made”(p. 5 fifth bullet). “In good time” could be read as if there should be a separate precontractual phase of information provision around investment decisions before the investor can choose the investment product in a second part of the process. We are not in favour of such an artificial splitting up of the process of information provision in two steps. The KID should be part of the usual information exchange leading to the signing of a contract. Moreover, it should be clear that the fact that a product is within the scope of PRIPs or that a KID has to be provided, should not necessarily mean that an activity of “advice” (in the sense given by MiFID) has been carried out. The concepts of “advice” and “commercialisation” should follow the rules derived from MiFID. PRIPs intends to offer investors more and better information for “packaged” or “wrapped” products but without prejudging the nature of the relationship with the client.
We welcome the option to have marketing tools at the side of the KID.

The summary of the prospectus should not take elements of the KID, because the prospectus is an instrument of disclosure for the issuer whereas the KID focuses on product information at the point of sale having a meaning which is different from the highly complex prospectus and its summary (see COM(2009) 491 final). Prospectus Directive´s provisions are to be kept within their product scope, accordingly to EU legislation.

The necessary disclaimer for the liability of the responsible producer of the KID is not mentioned in the document, but nevertheless very important. The short form of the KID enhances the risk of having not dealt with all aspects of the product as it would be the case in a full prospectus. This risk of having not delivered a full description of the whole profile of the product should be covered by the disclaimer. Because of its importance, it should have an own bullet point at the end of the document.

Elements of PRIPS products like guarantees, capital protection, inclusion into the compensation schemes, collaterals should be taken into account by the PRIPS regime and lead to a clearly separated version of KID and a lighter degree of disclosure. Consumer testing and past experience proved that few problems arise when capital protection exists and only the expected return is at risk. That evidence deserves to be taken into account when defining the legal frame for such capital protected products. We even argue for an exclusion of deposits from the scope of PRIPs due to their special features in terms of investors protection within the Deposits Protections Schemes.

The definition of being wrapped is to be taken into account. Simpler products being easily understandable merit a different approach. Otherwise, it would not only impose an unnecessary and costly burden to the industry, but will neither result in better consumer protection nor make investor's understanding of this "plain-vanilla wrappers" less difficult.

7. **Would you agree that these are the key areas in which comparisons are important for investors? How can these be best disclosed so as to aid comparisons? Are there other areas which might be equally important?**

KIDs should not need a previous approval, that would be an unnecessary bureaucratic hurdle and an obstacle to product innovation and flexibility.
On costs, the KID should show distribution costs, not manufacturing costs. MiFID as the benchmark for cost disclosure does not need any revision in this regard.
On liquidity, this item needs explanation because, although the KID could provide the client with information on the existence of a secondary market, a general classification of a product as liquid or non-liquid can be misleading. Such an explanation cannot be done in the KID, it is part of investment advice. The KID is only a building block within an ensemble of measures to improve the information base of the investment decision, - like prospectuses, information brochures and, last but not least, financial education.

8. **What elements of the KID might need to be different for different classes of PRIP? E.g. for retail structured products, insurance-based PRIPs or nonharmonised funds?**

Existence of secondary market or not could be a criterion to separate classes of PRIPs existence of guarantee covered by compensation scheme national legal frameworks has to be taken into account for the KID, f. e. guaranteed interest for insurances etc., for retirement provision products f. e. which have already to fulfill duties of information the type of the structure ("packaged" vs. "wrapped").

9. **What are the classes or types of PRIP for which differences might be necessary?**

PRIPs products with capital guarantee should be subject to a different treatment. It would be important to focus on the perspective of investors and whether they understand the product. It might be necessary to distinguish between "packaged" and "wrapped" products from this perspective. Even if the structure of some wrapped products might be complex they are easy to understand for investors and therefore do not deserve to be included.

10. **How far might the KID for PRIPs be harmonised for products that are not harmonized at the European level?**

The harmonization of he KID for PRIPs can only take place on a very generic level of having a (narrative) description of product, producer, risk, benefit, liquidity and costs. A further standardization would be overambitious because of the lack of product harmonization.

11. **Do you agree that requirements on pre-contractual disclosures should be directed at the product originator? Are there any practical issues to be considered with this approach, e.g. where individual products are not**

intended for retail clients, or where a distributor is able to add margins to a product, changing its cost structure? How can it be best ensured that retail clients buying PRIPs are always given a KID?

EACB agrees. The fact that the distributor gets something for selling the product should not be seen as repackaging/ remanufacturing. Investment firms are already obliged to give the customer adequate information so that the KID will be another means to fulfill this duty. In any case, cooperation of manufacturer and distributor will be needed contractually so that the details can be cleared with regard to the delivering of the KID to the customer. Therefore, a separate regulation by the European legislator will not be needed because the solution is up to the normal negotiations between market partners.

12. **How should wrappers be handled so as to ensure investors receive information that is comprehensible to them and which they can use to compare PRIPs?**

n/a

13. **Are there special cases that need particular treatments? E.g. in some Member States a single wrapper may provide access to a very wide of underlying assets or products, including hundreds of funds.**

n/a

14. **What are the issues with applying MiFID selling rules to the distribution of insurance-based PRIPs and banking-based PRIPs (e.g. structured term deposits)?**

15. **Are there any refinements to the MiFID handling of conflicts of interest that should be considered for PRIPs?**

EACB argues for not changing the scope of MiFID provisions to include the up to now not covered PRIPS products. MiFID already states that investors should be given all relevant information and it states the obligations to know the specific needs, risk profile and circumstances of investors (test of appropriateness and suitability) depending on the type of service/product offered and the client categorisation. The PRIPs initiative aims at clarifying which information the investor should be given in the case of PRIPs products, but should not change the following MiFID definitions:

- what is advised/non-advised selling
- when should a suitability test be conducted
- when an appropriateness test should be conducted.

With regard to PRIPS products being complex or non complex we would like to refer to the MiFID already stating what is „complex“ and „non-complex“. This MiFID definition should not be affected by the PRIPs measure. Furthermore, there are other important criteria when approaching from a practical point of view the issue of consumer protection: it is not only intrinsic „complexity“ what should matter, but also the practical and day-to-day facts of the real problems of consumer protection and confidence which arise from each type of product. EACB is of the opinion that products with capital protection and/or being in fact „plain vanilla“ wrappers do not involve potential conflicts with regard to investor protection and therefore it should be legitimate to be kept out of any „complex product“ added regulation, such as appropriateness tests.
Also in respect of the handling of conflicts of interest the MiFID should be the benchmark.

16. Should the general duty to act in the best interest of the client constitute a common overarching principle for all PRIPs?

EACB agrees.

17. How can the nature of the services being offered by the seller be best communicated? Should the client be informed if the recommendations are based on a broader or more limited range of products?

Again MiFID should be the benchmark. EACB does not see the need to inform the client about the range of products offered. The debate on open architecture should not be started again because of the very clear MiFID regulation in this regard. Article 19 para. 1 and 2 of Commission Directive 2006/73/EC.

18. Should those making recommendations comply with specific comparable reporting obligations to clients, e.g. on the underlying reasons underpinning the advice, as is currently the case in the IMD?

EACB likes to reiterate that MiFID should be the benchmark to guide investment advice and commercialisation activities.

19. What information do retail investors need about remuneration and costs, so as to combat so-called 'commission bias' and enable informed decision making?

20. Would a more standardised approach to cost and remuneration disclosure tested on consumers help?

Again MiFID encloses encompassing regulation in this regard (see Art. 19 para. 3 MiFID in connection with Art. 33 of Commission Directive 2006/73/EC. EACB does not see any need for alteration. See also our response to question 21.

21. Do you agree that direct sales should be covered by PRIPs sales rules? Should rules be only tailored in so far as this allows differences in the risks to consumer protection found in different channels to be reflected?

Yes. MiFID covers this already, e. g. demands that investment firms should prepare the management of conflicts of interests to avoid conflicts with regard to the payment of boni (see Art. 21 literal (b) of Commission Directive 2006/73/EC)

22. Should a suitability, or at the least an appropriateness test, always be required when selling PRIPs, or only for some PRIPs?

EACB strongly disagrees with this. See our previous comments on this topic. MiFID states no obligation for investment advice. Only in case the investment firm offers advice to the investor it is obliged to perform a suitability test. In this regard the last sentence in chapter 4.6 and the beginning of chapter IV speaking of "an assessment of the adequacy of the product for the investors' needs may be required in some circumstances" in the case of non-advised sales (see sentence 2 of the third bullet point under Principles in the grey box) could be read as arguing for an obligation to investment advice. Furthermore, we refer to our answers to questions 14, 15 and 23 of this document.

23. Are there any issues to be addressed when applying the MiFID approach towards the concept of retail client across the whole PRIPs market?

No. EACB thinks that the MiFID concept of the classification of clients should be used generally but feels the need to scrutinize whether there should be exemptions for specific classes of PRIPs products. See also our remarks to question 14.

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