Frankfurt am Main,
27 September 2018

BVI's response to the FCA Call for Input "PRIIPs Regulation – initial experiences with the new requirements"

BVI[1] noted with great interest the FCA's initiative seeking input from market participants and consumers about their initial experiences with the PRIIPs regime. Indeed, since its entry into force at the beginning of 2018 fund management companies represented by BVI, but also distributors and retail investors, are all struggling with application of the new requirements and the outcomes they generate. The market experience in the first eight months shows a clear need for discussing, assessing and reviewing the functioning of the PRIIPs framework. However, given that PRIIPs is based on EU rules and formed in detail by directly applicable Level 1 and 2 Regulations, a review of the applicable legal framework can only be conducted at the EU level. Therefore, while appreciating the FCA's initiative, we will further engage with the EU institutions in order to prompt a timely official review of the PRIIPs regime as foreseen in Article 33 of the Level 1 Regulation.

Nonetheless, we would like to raise your attention to one particular aspect of the FCA's paper which is based upon an erroneous reading of the PRIIPs rules. In paragraph 3.18, the FCA assumes that non-standardised OTC derivatives qualify as "other assets" for the purpose of transaction costs calculation under PRIIPs. As a consequence, the results of such calculation shall supposedly be subject to the limitation in Annex VI point 20 of the PRIIPs RTS meaning that the calculated transaction costs must not be less than the amount of actual identifiable transaction costs.

This conclusion is clearly wrong. Derivative instruments are generally not treated as "other assets" under Annex VI of the PRIIPs RTS regardless of their trading habitus or the level of standardisation. Instead, they are subject to a specific provision in Annex VI point 16. This paragraph is relevant for the calculation of transaction costs for all types of derivative contracts listed under MiFID II. It also accounts for all relevant instrument structures by stipulating particular calculation requirements for standardised exchange-traded derivatives (subparagraph a)), linear non-standardised instruments (subparagraph b)) and non-linear ones (subparagraph c)). The provision in subparagraph b) explicitly targets situations "where there is no price transparency or regular trading in the instrument itself" and thus, refers clearly to non-standardised OTC derivatives. Hence, even though in principle non-standardised OTC derivatives might have qualified as "other assets", they have been regulated in point 16 of Annex VI which must be considered an exhaustive "lex specialis". Since point 16 is embedded in the section for transferable securities and other instruments with frequent trading opportunities[2], the limitation in point 20 does not apply.

Notwithstanding these legal arguments, a reference to point 20 Annex VI in relation to non-standardised OTC derivatives is also pointless from the practical point of view. Transactions in such instruments do not involve explicit costs in terms of trading or clearing. In particular, non-standardised OTC derivatives

[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Fund companies act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's over 100 members manage assets of more than 3 trillion euros for private investors, insurance companies, pension and retirement schemes, banks, churches and foundations. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

[2] Cf. Point 9 Annex VI of the PRIIPs RTS.

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are not yet subject to a clearing obligation under EMIR. Therefore, there are generally no actual identifiable costs associated with transactions in non-standardised OTC derivatives which might be treated as a lower limit in accordance with point 20 Annex VI of the PRIIPs RTS.

We trust that our comments will prove convincing and will persuade the FCA to allow for a long overdue open debate on the practical impact and drawbacks of the PRIIPs transaction costs methodology.