



Regulatory Newsflash

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On 14 September, the EU Parliament rejected the EU Commission's Delegated Regulation on the Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs) and on 15 September 2016, the Belgian Financial Services and Markets Authority (FSMA) published a communication on the reporting obligation regarding insurance transactions related to investment funds.

We provide you with some more information on both of these publications.

We wish you a pleasant reading.

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1. PRIIPs delay looking more likely but implementation timeline still challenging

On 14 September, the EU Parliament [voted](#) to reject the EU Commission's [Delegated Regulation](#) on the Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs). This is

the first time that the EU Parliament has formally rejected technical rules on financial services legislation. The Delegated Regulation, based on the final draft [Regulatory Technical Standards](#) (RTS) prepared by the European Supervisory Authorities (ESAs), dated 31 March 2016, was rejected as “so flawed and misleading that it could actually lose [retail investors] money”. MEPs overwhelmingly passed the resolution rejecting the RTS (by 602 votes to 4, with 12 abstentions), calling for the EU Commission to submit a new RTS taking into account the EU Parliament’s concerns about the text. The Parliament also called on the EU Commission to postpone the application date of PRIIPs.

The PRIIPs Regulation requires that firms who manufacture, sell or advise on PRIIPs products (including investment funds, life insurance policies with an investment element, derivatives, structured products and structured deposits) must provide retail investors with a Key Information Document (KID). As such, the Regulation will apply to a wide range of firms, including banks, insurers, and investment managers. The RTS covers the presentation, content, review and provision of the KID, including the methodologies for risk and reward and cost calculations.

Will PRIIPs be delayed?

- PRIIPs is currently scheduled to apply to firms from 31 December 2016. It is possible that the RTS could be redrafted and agreed on an accelerated timescale e.g. in a matter of weeks, rather than months. However, this is unlikely given the process involved in finalising the RTS (discussed below).
- Consequently, the EU Parliament called on the EU Commission to consider a proposal postponing the application date of PRIIPs (without changing any other provisions in the level 1 text and therefore not opening any fundamental debates on the text) in order to ensure smooth implementation of the requirements and to avoid firms having to comply with the Regulation without the technical standards being in force in advance.
- The EU Parliament's vote does not formally delay the Regulation. A delay to PRIIPs would require the EU Commission to bring forward a new legislative proposal in order to change the level 1 text. The EU Commission is not obliged to do this and has previously expressed reluctance to bring forward any delay to PRIIPs. However, it will come under increasing pressure to do so, making a delay to PRIIPs a likely outcome in the event that the EU Commission cannot quickly satisfy the EU Parliament's expectations.
- During the Eurofi Financial Forum conference on 8 September, the Chair of the European Insurance and Occupational Pensions Authority (EIOPA), Gabriel Bernardino, stipulated that he would like a nine month delay to the introduction of the Regulation. Another possible option would be to align the PRIIPs application date with that of MiFID II (i.e. 3 January 2018). This would be welcomed by firms, given the level of cross-overs there are between the two pieces of legislation.

What areas has the EU Parliament requested the EU Commission address in a revised RTS?

- **Comparable products:** consumer information on investment products should be comparable to promote a

level playing field in the market, regardless of the type of financial intermediary which manufactures or markets them.

- **Calculation of risk:** it is misleading to investors to remove credit risk from the calculation of risk categorisation of insurance products.
- **Multi-option products:** the treatment of multi-option products should be clarified, particularly in relation to the explicit exemption granted to UCITS funds under the PRIIPs Regulation.
- **Calculation of future performance scenarios:** flaws in the methodology for the calculation of future performance scenarios do not fulfil the requirement under PRIIPs for information that is “accurate, fair, clear and not misleading”. In particular, it does not show for some PRIIPs, even in the adverse scenario, and even for products which have regularly led to losses over the recommended minimum holding period, that investors could lose money.
- **Comprehension alert:** the lack of detailed guidance on the “comprehension alert” creates a serious risk of inconsistent implementation of this element in the KID across the Single Market. Therefore, further standardisation of when the comprehension alert will be used should be introduced.
- **Spirit of PRIIPs:** left unchanged, the rules in the RTS risk going against the spirit and aim of the legislation, which is to provide clear, comparable, understandable and non-misleading information on PRIIPs to retail investors.

What does this mean for firms?

The fundamental requirements of the Regulation will not change. Firms should not pause in their PRIIPs implementation as, at this stage, it is not certain that there will be a delay and so continuing implementation is the conservative course of action. Firms will still need to produce KIDs and invest resources into ensuring compliance with these requirements. In the event that a delay is agreed, this will only provide a short breathing space, given the complexities involved in PRIIPs implementation and the fact that firms must also implement product governance requirements under MiFID II by 2018.

Currently, it is not yet clear precisely how the EU Commission may choose to redraft the RTS to take into account the EU Parliament’s concerns. However, in this uncertain environment, firms can still take “no regrets” actions in all other areas related to PRIIP compliance and preparation – template creation, product scripting, risk methodologies, costs, credit risk, technology infrastructure and software development, market data orchestration, KID production operating model and sales cycle delivery and customer journey.

Next steps

- The EU Parliament has called on the Commission to redraft the RTS. The Commission will send the RTS back to the ESAs for revision, who will then send the redrafted RTS back to the Commission for endorsement. In theory, the Commission then has three months to decide whether or not to adopt the RTS. Upon adoption, the scrutiny for the Parliament and the Council starts anew. This will be one month if no substantial changes have been made by the Commission, or three months if the RTS have been changed. However, as this is the first time that the EU Parliament has formally rejected technical rules on financial services legislation, this is uncharted territory. Therefore, it is

possible that the institutions could agree an accelerated timetable informally.

- The Council of the EU held a [silence procedure](#) on the RTS on 15 September, during which 19 delegations (accounting for 59.49% of the total population of the EU) indicated their intention to object to the RTS. This fell short of the qualified majority. Therefore, it was suggested that Coreper invites the Council to confirm that it has no intention to object to the RTS.

If the Commission does determine that a delay of the PRIIPs package is necessary, it will need to prepare a legislative proposal which sets this out. The text of the proposal would then need to be agreed by the EU Parliament and Council separately and then as part of trilogue negotiations, before entering into force before the end of the year (i.e. the date on which the PRIIPs Regulation is currently due to apply to firms).

2. FSMA Communication on the reporting obligation regarding insurance transactions related to investment funds

Introduction

On 15 September 2016, the Financial Services and Markets Authority (FSMA) published its Communication_2016_15 on the reporting obligation regarding insurance transactions related to investment funds ([NL](#) / [FR](#)) (hereafter, the communication).

Purpose of the communication is to remind insurance companies of their reporting obligation and provide where necessary, further guidance. Additionally, the FSMA provides concrete recommendations to improve the quality and provision of these reports.

The basis for these recommendations can be found in a sector analysis performed by the FSMA on the annual and semi-annual reports to be drafted by insurance companies commercializing branch 23 life insurance products to retail investors.

The FSMA's analysis revealed that not all insurance companies draft annual and/or semi-annual reports and that some reports were of poor quality. The FSMA has in the meantime already discussed the relevant shortcomings with the respective insurance companies and urged them to take some remediation actions, which led to higher quality reports.

Main principles set out in the Communication

The Communication provides some further guidance on (a) the format and provision of annual and semi-annual reports and (b) on the required content.

a) Format and provision of reports

- **Format:** A report should be drafted for every underlying investment fund. In case an insurance contract is linked with

multiple investment funds, the FSMA rejects the current practice to draft one report containing an overview of all possible underlying investment funds. A specific report should be drafted for the relevant investment fund itself. The FSMA also considers it insufficient to provide only the (semi-) annual reports of the underlying undertakings for collective investment (UCIs) or to replace the reporting requirement by the provision of periodical factsheets, product sheets, or other information.

- **Provision of the reports:** These reports should be made available at the insurance company's registered offices. However the FSMA recommends to also publish them on the insurance company's website.

b) Content of the reports

- **Composition of the investment fund:** The FSMA considers it to be insufficient to limit the information on the composition of the investment funds to the enumeration of the different UCIs (UCITS or AIF) and recommends a 'look-through' approach providing information on the assets of the underlying UCIs.
- **Composition of the portfolio:** In order to have a concrete view of the portfolio at reporting date, a breakdown of the portfolio and the movements within the portfolio is to be provided. FSMA recommends to provide an overview of the movements within the underlying UCIs, complemented with graphs and tables on the actual composition of the portfolio, including the relevant geographic, monetary, sectoral, qualitative,... criteria.
- **Transactions in derivatives or foreign currencies:** The FSMA concluded that this information is often missing in the reports. Furthermore, a common mistake made, especially in case of investment funds with only one underlying UCI, is to copy the amount of the obligations of the underlying UCI. This amount would not correctly represent the obligations of the investment fund, since the investment fund is rarely the only investor in the UCI. The amount of the obligation should reflect the percentage of participation of the investment fund in the underlying UCI or financial instrument. Regarding the obligations deriving from foreign currencies FSMA recommends to use the applicable exchange rates at the moment of reporting.
- **Overview of the investment objectives:** the regulator clearly recommends to explain the investment objectives and functioning of the investment fund a lot better. It is not enough to 'copy/paste' the investment objectives of the underlying UCI's since this does not necessarily correspond to the investment objective of the "insurance" investment fund.
- **Description of the risks:** Similar to the comment on the investment objectives, the (semi-) annual reports should contain a description of the relevant risks of the investment fund and should take into account the relevant characteristics and composition of the investment fund (instead of copy/pasting from the underlying funds).
- **Evolution of the investment fund's value:** The reports should reflect the evolution of the value of the investment fund's units over a sufficiently long period. To enhance the uniformity of the reporting on this topic FSMA recommends to include the start date of the investment fund and, where possible, to describe the evolution of the unit's value over the same period as this is required for the underlying UCI's.

Contact

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