

CESR's Level 3 guidelines on the selection and presentation of performance scenarios in Key Investor Information (KII) for structured UCITS

The ABI's response to Consultation Paper CESR/10-530

About the ABI

The ABI is the voice of the UK's insurance, investment and long-term savings industry. It has over 300 members, which together account for around 90% of premiums in the UK domestic market.

The UK insurance industry is the third largest in the world and the largest in Europe, helping individuals and businesses protect themselves against the everyday risks they face. It pays out over £230 million per day in pension and life insurance benefits and over £50 million per day in general insurance claims. The industry is an important contributor to the UK's economy: it manages investments of £1.5 trillion, over 20% of the UK's total net worth; employs more than 300,000 people in the UK alone; is the fourth highest contributor of corporation tax; and is a major exporter, with one-fifth of its net premium income coming from overseas business.

1. Do you agree with the proposals in Box 2?

No. The guidelines confuse, rather than clarify, the requirements on firms, particularly in regard to the provision of information on performance scenarios. For example, point three states that firms "shall illustrate...the functioning of the formula in unfavourable, favourable and medium market conditions." Terms such as "favourable" and "unfavourable" are subjective and imprecise. It is likely that firms would have different interpretations of the terms and this has the potential to create confusion, for both firms and consumers.

Furthermore, the use of "unfavourable", "favourable" and "medium" does not reflect the language used in Article 36.3 of the regulation which states that "appropriate scenarios will be chosen to show the circumstances in which the formula may generate a low, medium or a high return". A performance scenario based on unfavourable market conditions may be significantly different to one based on low returns since different factors may be taken into account.

Similar confusion arises in point four of the guidelines which state that scenarios will be based on "reasonable assumptions". However, Article 36.5 of the regulation states that scenarios should be based on "reasonable *and conservative* [author's emphasis] assumptions". The inclusion of the term "conservative" is key since it may require firms to err on the side of lower assumptions about future market conditions and price movements.

The guidelines do not offer any additional clarity for firms and could, in fact, cause uncertainty about the information they are required to provide.

2. Are there any other scenarios which these guidelines should address?

No comments.

3. Do you agree with the proposals in Box 3?

The ABI does not have any particular concerns about the contents of Box 3 and we welcome that the guidelines give firms the freedom to decide between presenting the illustrative examples as graphs or tables.

While we welcome the provision of examples, we do have some concerns about those provided. The guidelines would be more instructive if they presented good and poor practice examples as this would give firms a much clearer picture of how to go about drafting them.

Many of the explanations offered in the examples conflict with advice on the use of plain language. For example, "If units are sold before the end date: the price will not be calculated using the formula but will be based on the net asset value of the UCITS which will include the market value of the financial derivative instruments used." Where the inclusion of such explanations is mandatory, the guidelines should present them in accordance with guidelines on the use of plain language. This would help firms get a better understanding of how to present such information.

ABI members have also raised concerns that the graphs, in particular, may prove to difficult for consumers to understand as they are hard to interpret.

4. Is there any other guidance which should be given about the presentation of scenarios?

See response to question 3.