



March 2011
AK Position Paper

Packaged Retail Investment Products Initiative
(investment products for small investors)

Position on the Proposal of the European Commission

About us

The Federal Chamber of Labour is by law representing the interests of about 3.2 million employees and consumers in Austria. It acts for the interests of its members in fields of social-, educational-, economical-, and consumer issues both on the national and on the EU-level in Brussels. Furthermore the Austrian Federal Chamber of Labour is a part of the Austrian social partnership.

The AK EUROPA office in Brussels was established in 1991 to bring forward the interests of all its members directly vis-à-vis the European Institutions.

Organisation and Tasks of the Austrian Federal Chamber of Labour

The Austrian Federal Chamber of Labour is the umbrella organisation of the nine regional Chambers of Labour in Austria, which have together the statutory mandate to represent the interests of their members.

The Chambers of Labour provide their members a broad range of services, including for instance advice on matters of labour law, consumer rights, social insurance and educational matters.

More than three quarters of the 2 million member-consultations carried out each year concern labour-, social insurance- and insolvency law. Furthermore the Austrian Federal Chamber of Labour makes use of its vested right to state its opinion in the legislation process of the European Union and in Austria in order to shape the interests of the employees and consumers towards the legislator.

All Austrian employees are subject to compulsory membership. The member fee is determined by law and is amounting to 0.5% of the members' gross wages or salaries (up to the social security payroll tax cap maximum). 560.000 - amongst others unemployed, persons on maternity (paternity) leave, community- and military service - of the 3.2 million members are exempt from subscription payment, but are entitled to all services provided by the Austrian Federal Chambers of Labour.

Herbert Tumpel
President

Werner Muhm
Director

Executive Summary

- The AK welcomes the intention linked with the PRIIPS initiative to increase investor information and consumer protection.
- The AK is in favour of primarily designing products in a simple and comprehensive manner - and not only the product-related information.
- The AK welcomes the intention that pre-contractual information for complex investment products shall be comprehensively standardised resp. harmonised to facilitate the comparison of products.
- The AK welcomes a broad scope for investment products, which can be classified as Packaged Retail Investment Product.
- The AK is in favour of standardised pre-contractual information (product information sheets) for all investment products, which are offered to small investors.

The AK position in detail

Questions

Q. 1: Should the PRIPs initiative focus on packaged investments? Please justify or explain your answer.

Q. 2: Should a definition of PRIPs focus on fluctuations in investment values? Please justify or explain your answer.

Q. 3: Does a reference to indirectness of exposure capture the 'packaging' of investments? Please justify or explain your answer.

Q. 4: Do you think it is necessary to explicitly clarify that the definition applies to fluctuations in 'reference values' more generally, given some financial products provide payouts that do not appear to be linked to specific or tangible assets themselves, e.g. payouts linked to certain financial indices, the rate of inflation, or the overall value of a fund or business?

Q. 5: Do you have any other comments on the proposed definition? If you consider it ineffective in some regard, please provide alternatives and explain your rationale in relation to the criteria for a successful definition outlined above.

On Questions 1 - 5:

Over the past years, packaged investment products have increasingly gained in significance. This product category, which is often difficult to understand for investors, does in particular include life insurance products, whose savings portions of the premium is invested in an investment fund or a basket of investment funds (unit-linked life insurances), index-linked life insurance, where the insurance payouts in the event of death or on maturity are linked to the performance of an index. Both in the case of the index and the unit-linked life insurance it is also possible to agree on guaranteed payouts. Depending on the agreement, the policyholder might be burdened with the risk of losses. But investment-oriented life insurances, which only provide for the agreement on a special investment strategy of the policyholder with the insurer as well as savings deposits, whose interest rate is linked to an index or stock basket, have also expanded the investment spectrum.

In the opinion of the AK, certificates - classified according to risk - must be rated as investment products, which can be hardly comprehended by the normal investor. This will not change despite the fact that capital protected certificates exist, which are often advertised with the apparent quality seal "100% Capital Guaranteed". In particular certificates without capital protection, such as discount certificates, bonus certificates or reverse convertibles are not easy to understand for little experienced small investors.

Over the past years, investment products have increasingly gained in significance

The AK is in favour of bank and investment products are being designed as clear, simple and comprehensible as possible

As AK investigations have shown, the lack of transparency is mainly a result of the information policy of the banks.

The AK has examined pre-contractual information for complex investment products in advisory discussions, on homepages as well as in adverts within the scope of a study ("New savings and investment products sold by the banks, October 2010"). A significant finding of this study was that many banks focus on capital guaranteed insurance products, such as index-linked life insurances, which are far too complicated and in most cases difficult to understand. At the time the survey was carried out, the focus was very much on "security" so that all products were sold with capital guarantees. However, the details of the guarantors were mainly hidden in the small print, and interest rates, yields or guaranteed amounts were frequently - quite often in a misleading manner - compared with savings book interest rates (e.g. "guaranteed interest rate pa in the comparison of savings books).

The Federal Chamber of Labour is in favour of bank and investment products are being designed as clear, simple and comprehensible as possible. A conclusion from the financial crisis is therefore that small investors have bought many products, where not only the information in pre-contractual advisory discussions and the accompanying written information were inadequate, but where the product structures including all objectively existing risks were too complicated.

That is why the AK is in favour of offering small investors products, which are less complex. The AK welcomes the circular, which the Austrian Financial Market Authority (FMA) recently sent to all Austrian credit institutions, according to which savings deposits in accordance with the Banking Act should remain simple and easy to understand. The FMA pointed out that the calculation of interest rates at any time represents an element of the savings book. Products, which provide for "interest rates", which depend on the performance of individual securities or indices, do in general not fulfil the legal requirements of the Austrian Banking Act. The FMA regards in particular a guarantee certificate in form of a savings certificate or products, which provide for a certain "bonus", which is for example dependent on the performance of a stock basket or an index as incompatible with the provisions of the Banking Act (Source: Circular of the Financial Market Authority on the structure of savings certificates pursuant to §§ 31 and 32 BWG, January 2011).

Therefore the AK is in favour of the principles of pre-contractual information, which were developed in the PRIIPS initiative not only to be applied to packaged products, but to all forms of savings and investments.

Small investors are not able to cope with a limited scope as they cannot differentiate between products themselves and are therefore not in a position to judge whether the required pre-contractual information they received has been correct and complete.

Questions

Q. 6: Should simple (non-structured) deposits be excluded from the scope of the initiative? Please justify or explain your answer.

Q. 7: Do you consider option 1 or option 2 preferable for achieving this? Please explain your preference, and set out an alternative if necessary, with supporting evidence.

Q. 8: Should such an exclusion be extended to financial instruments which might raise similar issues as deposits (e.g. bonds), and if so, how might these be defined? Please justify or explain your answer.

Investors, who come to the AK advice office, are often not even aware which product type they have obtained or who exactly their contractual partner is (Bank? Insurance? Investment company?)

On Questions 6-8

Another area of application - including simple saving products - is to be welcomed, because the private investor in general differentiates very little with regard to the product category for his investment. Small investors regard the various investment products as "savings products", irrespective of whether they are provided by a bank, an insurance company or an investment company. Apart from that, so-called simple savings products are becoming increasingly more complicated, which is a result of comprehensive interest rate adjustment clauses, different interest scales (in case of premature termination) for tied-up savings deposits or various offsetting methods for expenses (transaction fees, possible free transactions) in case of savings accounts with direct banks.

Consumers mainly focus on the investment purpose resp. the investment motive (for example saving for children, private pension etc.) as well as on yield, risks and liquidity (term, terminability); preferences in favour or against a certain product category only take second place and are less important than the criteria, mentioned above.

Investors, who come to the AK advice office, are often not even aware which product type they have obtained or who exactly their contractual partner is (Bank? Insurance? Investment company?). A common motive (stated in the AK advice office) why small investors decide in favour of a particular investment is the motivation to generate an added value, which goes beyond the interest return of a simple savings deposit; however, if possible, the risk should be readily comprehensible and ideally remain at the same level as that of a savings deposit. Hence, small investors can generally be regarded as averse to risk. Therefore, from the point of view of the AK, a very fine differentiation into PRIIP or Non-PRIIP does not really lead anywhere because it does not address the considerations of the small investor as which product he should choose - How profit-yielding is the product? How risky is it? What about terminability / term? In order to provide a clear standard, which gives small investors orientation and clarity, standardised product information sheets should be made available for all savings and investment products. Right at the top of this product information sheet should be the product category and the product provider.

The AK is in favour of providing small investors with short, simple and comprehensible documentation

Questions

Q. 9: Should pensions be explicitly excluded from the PRIPs initiative at this stage? Please justify or explain your answer.

Q. 10: Should annuities be treated in the same fashion? Again, please justify or explain your answer.

Q. 11: Do you have any comments on the proposed manner of achieving this exclusion?

Q. 12: Do you agree that variable annuities might need to be treated as a special case? If so, how should these be defined, and how do you think they should be addressed?

On questions 9-12

Small investors acquire a wide range of investment products - from "safe" to "risky" - under the aspect of pension provision. The investment motive "pension provision" is not suitable as a selection criterion whether a product should be a PRIP or a Non-PRIP. The AK is in favour of the idea that the clear assignability (to a product category), comprehensibility (of the cornerstones of the investment) and the comparability (with other products, also of other product categories) should be the objectives of standardised pre-contractual information.

Questions

Q. 17: Should the design of the KIID be focused on delivering on the objective of aiding retail investment decision making? If you disagree, please justify or explain your answer.

Q. 18: Should the KIID should be a separate or 'stand alone' document compared with other information that might be necessary, e.g. background information, other disclosures, or contractual information? Please justify or explain your answer.

Q. 19: What measures do you think will be necessary to ensure KIID remain streamlined and focused solely on key information?

On Questions 17-19

The AK is in favour of providing small investors with short, simple and comprehensible documentation. The strength of this information is useful for the small investor, but also to the intermediary, who can use this documentation as reliable advisory support.

In its advice office, the AK has time and again come across consumers resp. investors who often do not even know which type of product category they have acquired. Many investors are looking at their investments for

The AK regards it as necessary that the Financial Market Authority exercises control to supervise the implementation of the product information sheets of the product providers

the first time to find out, which cornerstones define their investments, when they have suffered a loss. Within the scope of this reflection process, why (high) losses or even a loss of capital occurred, suddenly the (open and until then not clearly answered) question emerges which type of product had been bought and who the actual contracting partner is. If the information the investor is provided with is clear, he is in no doubt whether his investment is with a bank, an insurance company or an investment company; this clearly conveyed knowledge - under aspects of the customer spreading the risk between various product providers - can also be important for an existing or future (sensible) investment decision.

The product information sheet should be coherent with all other product information (advertising, direct mailing, issue prospectuses) and contain no other misleading information (in particular in relation to the issue prospectus); coherence to issue prospectuses can be achieved if the product information sheet refers to the issue prospectus in a prominent place in order to draw the attention of the prospective investor to further resp. detailed information regarding the cornerstones of the investment or the identity of the product provider.

On questions 20-24 resp. 25-26

The AK is in favour of standardising the product information sheet to the highest degree possible.

What is required is catalogue of points covering all product areas, which is reflected in all product information sheets:

- Product description, structure and objective
- Risks
- Yields
- Performance
- Costs

Apart from the fact that the description of the risks involved is a key issue, each pre-contract product information sheet should also include the term (fixed for months/years or flexible with termination options) as well as the conditions for termination the contract. The AK is therefore in favour of ensuring that for each investment product - irrespective of simple savings deposit or complicated investment product in a "package" with Underlying - the term of the product and the conditions for termination (both for the product provider and for the investors) are provided as standard.

The AK regards it as necessary that the Financial Market Authority exercises control to supervise the implementation of the product information sheets of the product providers.

Questions

Q. 27: Should product manufacturers be made generally responsible for preparing a KIID? Please justify or explain your answer.

Q. 28: Are you aware of any problems that might arise in the distribution of particular products should responsibilities for producing the KIID be solely placed on the product manufacturer?

Q. 29: If intermediaries or distributors might be permitted to prepare the documents in some cases, how would these cases be defined?

On Questions 27-29

The AK is in favour of the product providers being responsible for the preparation of pre-contract product information sheets. The product concept as well as the details of its structure are the responsibility of the product issuer, whilst the correct description of the product as well as providing the investor with the product information sheets should be part of the binding advisory duties of the intermediary. The fact that the intermediaries should be in charge of the written information, should from the AK's point of view be regarded with some caution, as the AK advisors time and again have come across product information prepared by intermediaries, the factual correctness of which is debatable and whose description does not follow unified quality standards. It

is rather to be feared that objective correct investor resp. product information will be distorted by advertising messages or "transformed" into pure marketing messages of the intermediary.

Fact is that the small investor requires product-related information concerning the intermediary. This concerns in particular fees, which might be charged by the intermediary.

Questions

Q. 32: Should the summary prospectus be replaced by the KIID for PRIPs? Please outline the payouts and disadvantages you see with respect to such an approach.

Q. 33: Should Solvency II disclosures provided prior to the investment decision be replaced by the KIID for PRIPs? Please outline the payouts and disadvantages you see with respect to such an approach.

Q. 34: Do you agree with the suggested approach for UCITS KIIDs?

Q. 35: Are there any disclosures, e.g. required by the existing regimes, which you believe the PRIPs KIID should not include, but which should still be disclosed, e.g. separately to the KIID? Do you have any practical examples for such elements?

The AK has therefore proposed to introduce a traffic light system

On Questions 32-35

The AK suggests that the product information sheet for the PRIPs can serve as a template for pre-contractual information for all savings and investment products.

On Questions 36-37, 38-39, 40-41

The AK has suggested - as a direct consequence of the financial crisis - that all investment products should describe the associated risks as clearly as possible for small investors. The AK has therefore proposed to introduce a traffic light system, according to which the colours "red", "yellow" and "green" could signal the capital retention resp. the risk of total loss.

Performance is generally the eye catcher for investor interests. It would also be very welcome if performances would also be visualised as clearly as possible, for example by means of a bar chart. Descriptions of examples and scenario calculates might not be clear enough for small investors.

The effects of the costs on yield are a key information for the investor; after all the investor is most interested to know how much yield remains after (all) costs have been deducted (net yield). In view of the wide range of possible costs, which might incur once the contract is concluded and during the term, it would be welcomed if the costs would not only be itemised but if their effect on yield would also be explained.

From an investor's point of view, tax rates on yields also have to be regarded as a cost factor, whereby the need for information is based on the fact that taxes can be imposed on individual investment categories in different ways. Apart from that, all Member States have different tax regimes.

On Questions 42, 43:

Information on guarantees and guarantors is therefore a key issue because it represents a central product feature for (capital) security. For that reason - and in view of the importance small investors attach to this feature - information on guarantees/guarantors should be provided in a prominent place - and not in the small print. The AK advice office has records of a number of complaints concerning products, where details of the guarantor were only placed in the small print, i.e. hidden away. In a concrete case, the sales folder had advertised 100-percent guarantee, there would be no risk of loss in spite of the high yield potential. However, the guarantor was not mentioned once in the entire prospectus.

The AK welcomes in particular the circular of the Austrian Financial Market Authority (circular of the Financial Market Authority dated 2.12.2010 on questions of the prospectus right), in which it says under "Guarantee, Capital protection" that in order to avoid misleading guar-

antee statements in advertisements an explanatory reference should be included as who the guarantor is and what the capital protection is based on.

Supporting measures

Current problems - in particular conspicuous providers, products or company structures - should be addressed in a defined discussion scope and pursued if required or in case of doubt

The AK is in favour of efforts focussing on prevention work. The AK proposes to have an institutionalised dialogue between consumer protection, authorities, supervisory authorities and investor compensation authorities. Current problems - in particular conspicuous providers, products or company structures - should be addressed in a defined discussion scope and pursued if required or in case of doubt. Information on possible dysfunctional market practices could be conveyed to the supervisory and investor compensation authorities within the meaning of intensified cross-border cooperation. In particular the consumer protection authorities and organisations could - based on their experiences in advising consumers in financial services matters ("ear at the small investor market") - provide valuable information.

Should you have any further questions
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