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Agenda

- Setting the scene: PRIIPs summary
  - Key Information Document
  - Solutions ahead
What is the contribution of PRIIPs’ Regulation?
- PRIIPs, Packaged Retail and Insurance based Investment Products, is the first regulation on a European level to deal with pre contractual information.

What are the objectives of PRIIPs’ Regulation?
- Promote the emergence of a single European insurance market
- Ensure the comparability between similar products
- Improve transparency and increase investors confidence
- Harmonize the framework of administrative and financial penalties on a Europe-wide basis

How does PRIIPs’ Regulation attempt to achieve these objectives?
- By defining a KID (Key Information Document) with standard format and content
- By making it compulsory to provide this KID prior to any proposal or a contract
Setting the scene: PRIIPs summary

Types of product in scope

**ASSET MANAGEMENT**
- Structured deposits (but not deposits linked solely to interest rates).
- Products with capital and/or return guarantees
- All investment funds, including UCITS and retail AIF, whether closed ended or open ended
  - Investment funds dedicated to institutional investors

**BANKING**
- SPVs, holding companies
- Structured deposits (but not deposits linked solely to interest rates).
- Products with capital and/or return guarantees
- Derivative instruments
  - Deposits, bonds, shares

**INSURANCE**
- Unit-linked life insurance
- Certain pension products
  - Non life insurance products
  - Pension products
Setting the scene: PRIIPs summary

**Timeline**

- **Adoption of final version of the regulation**
  - 5 April 2014
  - 1 January 2017

- **Technical specification process**
  - 11/2014
  - 02/2015
  - 11/2015
  - 02/2016
  - 03/2016

- **Zoom on technical specification process**
  - Release of the Discussion Paper KID for PRIIPs
  - Feedbacks on Discussion paper by stakeholders
  - Preparation of draft Regulatory Technical Standards (RTS) by the ESAs
  - Consumer testing exercise prepared by European Commission
  - Consultation on the draft RTS
  - Draft RTS to be presented to European Commission

- **Entry into force**
  - 1 January 2017

- **Review after 4 years**
  - 1 January 2019

- **End of exemptions for UCITS**
  - 1 January 2020

- **Links**: Link'n Learn 2016 - PRIIPs
Following the publication of PRIIPs Regulation (EU) 1286/2014 on 9 December 2014, the European Supervisory Authorities (ESAs) have been mandated to draft Regulatory Technical Standards (RTS) on the content and presentation of the related KIDs.

As such, on the 11th November 2015 the ESA’s issued a joint consultation paper, followed by the final draft regulatory technical standards on 31st March 2016, which gives the industry a greater clarity on a number of key aspects of the regulation. In addition to the formulation of a draft of the first level 2 recommendations (RTS), certain key aspects, such as template design, clarification on the risk and performance sections are given.

An important step towards understanding the final requirements. The consultation paper is part of a wider effort, on behalf of the ESA’s to solicit feedback from the industry, as they formulate and add greater detail to the RTS

ESAs has submitted the RTS for endorsement to the European Commission on April 7 2016.
Setting the scene: PRIIPs summary

Main information

A person advising on, or selling, a PRIIP shall provide retail investors with the KID in good time before those retail investors are bound by any contract or offer relating to that PRIIP.

Maximum 3 A4 pages
Stand alone document
Consistent with marketing information

Easy to read, accurate and not misleading
Should be available in the language of the retail investor

Where applicable, a comprehension alert

Regular review of the content.
Revised version to be made available promptly.
## Setting the scene

Costs disclosure: UCITS KIID vs. PRIIPS KID vs. MIFID II

<table>
<thead>
<tr>
<th></th>
<th>MIFID II</th>
<th>PRIIPS(KID)</th>
<th>UCITS(KIID)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Format</strong></td>
<td>Expressed in monetary and percentage terms</td>
<td>Expressed in monetary and percentage terms</td>
<td>Expressed in percentage terms</td>
</tr>
<tr>
<td><strong>Methodology</strong></td>
<td>Ex-ante and ex-post</td>
<td>Ex-ante and ex-post</td>
<td>Ex-post</td>
</tr>
<tr>
<td><strong>One-off charges[1]</strong></td>
<td>To be disclosed</td>
<td>To be disclosed</td>
<td>To be disclosed</td>
</tr>
<tr>
<td><strong>On-going charges[2]</strong></td>
<td>To be disclosed</td>
<td>To be disclosed</td>
<td>To be disclosed</td>
</tr>
<tr>
<td><strong>All costs related to the transactions[3]</strong></td>
<td>To be disclosed</td>
<td>To be disclosed</td>
<td>Don’t have to be disclosed</td>
</tr>
<tr>
<td><strong>Incidental costs[4]</strong></td>
<td>To be disclosed</td>
<td>To be disclosed</td>
<td>To be disclosed</td>
</tr>
<tr>
<td><strong>Cost and charges to be aggregated</strong></td>
<td>All above mentioned costs</td>
<td>All above mentioned costs</td>
<td>No aggregation required</td>
</tr>
<tr>
<td><strong>Cumulative effect of costs on the return</strong></td>
<td>To be disclosed</td>
<td>To be disclosed</td>
<td>N/A as no aggregation required</td>
</tr>
</tbody>
</table>

[1] All costs and charges (included in the price or in addition to the price of the financial instrument) paid to product suppliers at the beginning or at the end of the investment in the financial instrument; Examples: Front-loaded management fee, structuring fee, distribution fee.

[2] All on-going costs and charges related to the management of the financial product that are deducted from the value of the financial instrument during the investment in the financial instrument.

Examples: Management fees, service costs, swap fees, securities lending costs and taxes, financing costs.

[3] All costs and charges that incurred as result of the acquisition and disposal of investments.

Examples: Broker commissions, entry- and exit charges paid by the fund, marks up embedded in the transaction price, stamp duty, transactions tax and foreign exchange costs.

Side question
Is the KID useful? Food for thought…

Link’n Learn 2016 - PRIIPs
Agenda

Setting the scene: PRIIPs summary

Key Information Document

Solutions ahead
PRIIPs affects Asset Managers differently depending on products and distribution model.

**Asset Managers**
- AIFs
- UCITS

**What changes?**
- data frequency
- SRI calculation
- performance scenarios
- RIY

**Investors**

**Data Transparency**
- Costs
- Risks
- Sensitivities
- Narratives

**Direct impacts**
- Pre-KID / contractual KID
- HWNI / retail timeline
- Input data & maintenance
- Dedicated / unit-linked products

**Indirect impacts**

**Life Insurer**

**What challenges for insurers?**
- Unit linked insurance products “ULIP”

**Link’n Learn 2016 - PRIIPs**
New KID Content Dissected
9 overall sections

1. Comprehension alert
   Where relevant

2. Identity information
   Information about PRIIP manufacturer and its competent authority

3. “What is this product?”
   Type of PRIIP, objectives, consumer type to whom PRIIP is intended to be marketed, information on insurance benefits, the term of the PRIIP

4. “What are the risks and what could I get in return?”
   Brief description of the risk-reward profile, containing: a summary risk indicator with supplementary explanations; possible maximum loss of invested capital; […]

Source: KID PRIIPs Factory Platform
New KID Content Dissected

9 overall sections

4. “What are the risks and what could I get in return?”
   [cont’d] performance scenarios; conditions for returns or performance caps; impact of tax legislation

5. “What happens if [name of the PRIIP manufacturer] is unable to pay out?”
   Brief description of whether the related loss is covered by a compensation or guarantee scheme, if so, which risks are covered and which not

6. “What are the costs?”
   Costs associated with an investment in the PRIIP, comprising direct and indirect costs, one-off and recurring costs with summary cost indicators and aggregate costs; an indication of additional costs charged by advisors, distributors etc. must be included
New KID Content Dissected

9 overall sections

7. “How long should I hold it and can I take money out early?”
   Applicable cooling off or cancellation period, minimum holding period, disinvestments before maturity, consequences of cashing in early

8. “How can I complain?”
   How and to whom complains can be made

9. “Other relevant information”
   Brief indication of any additional information documents, excluding marketing material

Source: KID PRIIPs Factory Platform
Quantitative challenges for risk, performance & costs disclosures for your KIDs

AIFs and UCITS

What is new for PRIIPs:
• Summary Risk Indicator (SRI) derived from a combination of Market and Credit risk assessment (where relevant)
• MRM class based on a different scale than SRRI and derived through Cornish-Fischer or Monte Carlo Value-at-Risk
• Performance scenarios computed similarly to Market Risk, and revision criteria
• Cost transparency and Reduction in Yield (“RIY”) 
• “Recommended holding period” to be defined
• Associated narratives (mandatory and ad-hoc)
• Structured Funds: transparency information from hedging counterparty may be required

What is carried over from UCITS KIIDs:
• Market risk indicator (MRM) from 1 to 7 derived from annualised volatility
• 4 months monitoring window, with associated triggers to update the KID and SRI

\[
q_{CF} = q + \frac{(q^2 - 1)s}{6} + \frac{(q^3 - 3q)k}{24} - \frac{(2q^3 - 5q)s^2}{36}
\]

\[
q_{CF} = -1.96 + 0.474s - 0.0687k + 0.146s^2
\]

\[
VaR_{CF} = \frac{\sigma^2}{2} N + q_{CF}\sigma\sqrt{N}
\]

\[
\sigma^* = -1.96 + \frac{3.84 - 2VaR_{CF}}{\sqrt{T}}
\]
Transparency challenges for supporting the KID production of your insurance investors

A UCITS KIID does not contain all the information needed to produce a ULIP KID

Data transparency requirements

Required content could include raw data:
- Total return **past performance**
- Portfolio benchmarks/proxies
- Portfolio allocations
- Portfolio credit rating limit
- Costs breakdown
- Potential associated **narratives**

And/or calculated data:
- **SRI**, or MRM and CRM
- **Performance percentiles** over different time horizons
- Portfolio’s **average credit rating**
- **Risk analytics**: volatility, skew, kurtosis, Value-at-Risk
- **Reduction in Yield**
- **Liquidity profile**

Classification

**Classification** of the ULIP may differ from the underlying UCITS

Reporting framework

**Data Exchange Templates** are being discussed (c.f. slide 17)

**Frequency** likely to be monthly / quarterly and following any material changes (risk, costs)

**Consistency** expectations and requirements with Solvency II and MiFID 2 disclosures

Synergies

- **Solvency II** (TPT): e.g. ex credit quality steps
- **UCITS SRRI** compilation and monitoring tools
Key Information Document
Risk & reward section

This section deals with different methodological options to elaborate the risk and reward information in the KID and different risk and reward presentations:

**Risk section**

Three main types of risks:
- Market risk
- Credit risk
- Liquidity risk

The proposed layout for the risk section entails:
- Two risks (market risk and credit risk) aggregated into an SRI
- Liquidity risk to be described in the risk narrative if relevant

**Reward section**

Selection of scenarios and calculation of performance implies a choice on:
- the general approach and methodology
- the time frame and holding period
- the payment and payout structures
- the percentages and nominal value
- the cost information on the performance presentation

**Risk indicator**

- Example

**Performance scenarios**

- Example
Summary Risk Indicator (SRI)
Where is the product in terms of Market and Credit Risk

**Market Risk Measure**
- PRIIPs can be assigned to seven MRM classes and for this purpose they are divided into four categories
- Category I PRIIPs are assigned based on qualitative criteria, while for Category II, III and IV the basis for the MRM is the Value-at-Risk @ 97.5%

**Credit Risk Measure**
- Credit risk shall be assessed when the return on the investment depends on the creditworthiness of manufacturer or the party bound to make the relevant payment to the investor
- On AIFs and UCITS credit risk shall be assessed on a look-through basis

**Aggregation to a single SRI**
- SRI is a guide to the product’s level of risk, helping the investor to assess it and compare it with other products
- It takes into account how likely the investor can lose money and the possibility to enter some form of protection

**Example of PRIIPs’ classification according to four categories (non-exhaustive list):**
- Category I: Where investors could lose more than the amount invested; Derivatives and PRIIPs with insufficient historical performance data or illiquid underlying assets
- Category II: PRIIPs which offer non-leveraged exposure to the prices of underlying investments, or with constant multiples; Standard unit linked products
- Category III: PRIIPs whose values reflect the prices of underlying investments, but not as a constant multiple of the prices of these underlying investments; Structured products
- Category IV: PRIIP whose value depends in part on factors not observed in the market. This includes insurance-based PRIIPs which distribute to retail investors a portion of the PRIIP manufacturer’s profits. Guaranteed Interest rate with Profit sharing

**Credit Quality**

<table>
<thead>
<tr>
<th>Credit Quality step</th>
<th>Credit Risk class</th>
<th>Rating Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>CR1</td>
<td>AA / AAA</td>
</tr>
<tr>
<td>1</td>
<td>CR1</td>
<td>AA</td>
</tr>
<tr>
<td>2</td>
<td>CR2</td>
<td>A</td>
</tr>
<tr>
<td>3</td>
<td>CR3</td>
<td>BBB</td>
</tr>
<tr>
<td>4</td>
<td>CR4</td>
<td>BB</td>
</tr>
<tr>
<td>5</td>
<td>CR5</td>
<td>B</td>
</tr>
<tr>
<td>6</td>
<td>CR6</td>
<td>CCC</td>
</tr>
</tbody>
</table>

**Market Risk**

<table>
<thead>
<tr>
<th>Credit Risk</th>
<th>MR1</th>
<th>MR2</th>
<th>MR3</th>
<th>MR4</th>
<th>MR5</th>
<th>MR6</th>
<th>MR7</th>
</tr>
</thead>
<tbody>
<tr>
<td>CR1</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>CR2</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>CR3</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>CR4</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>CR5</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>CR6</td>
<td>6</td>
<td>6</td>
<td>6</td>
<td>6</td>
<td>6</td>
<td>6</td>
<td>7</td>
</tr>
</tbody>
</table>

**Liquidity Risk:** for products tradable over their life but for which no regulated liquid market exists, a warning shall be included within the SRI, highlighting that selling the PRIIP before the RHP may not be possible and/or imply remarkable costs or losses.

**Narrative explanation:** it shall accompany the SRI and briefly explain its purpose, as well as the underlying risks and, where applicable, all material risks not adequately captured by the indicator

**Other warnings:** if issues on cashing-in before maturity or currency risks exist, they shall be properly mentioned and described
## Summary Risk Indicator (SRI)
### Market Risk Measure (MRM)

<table>
<thead>
<tr>
<th>Category</th>
<th>Description</th>
<th>Computation Methodology</th>
<th>MRM</th>
</tr>
</thead>
</table>
| Category I | Leveraged products<br>Derivative products qualifying as PRIIPs<br>PRIIPS for which the underlying or their proxies have prices on less regular basis than monthly, or they do not have a proxy | The MRM takes the value 6 or 7 based on qualitative criteria:  
- PRIIPS for which the underlying or their proxies have prices on less regular basis than monthly, or they do not have a proxy: MRM=6  
- If it is possible to lose more than the invested amount: MRM=7  
- Derivative products qualifying for PRIIPS: MRM=7 | 6 or 7 |
| Category II | PRIIPS that offer non-leveraged exposure to the prices of underlying investments<br>PRIIPS that offer leveraged exposure on underlying investment that pays a constant multiple of the prices | The methodology is based on the modified VaR of the historical returns  
- 2 years of daily prices or 4 years of weekly prices or 5 years of monthly prices are retained  
- The modified (Cornish-Fisher) VaR@97,5% is computed on the historical returns  
- The equivalent “Gaussian” volatility is derived from the VaR figure  
- A MRM class is derived from the corresponding volatility bucket  
- Where the fund displays insufficient history, a natural benchmark shall be defined | 1 to 7 |
| Category III | PRIIPS whose value reflects the prices of underlying investment, but not as a constant multiple of the prices | The methodology is based on the simulated VaR at maturity of the product  
- Perform 10,000 historical simulations of the value at maturity of the product  
- 5 years of historical market data is considered  
- Deduce the VaR @ 97,5% at maturity of the product  
- The equivalent volatility is derived from the VaR figure, corresponding to a volatility bucket | 1 to 7 |
| Category IV | PRIIPS that display no observable market factors that would permit the standard risk measurement as laid down in the RTS | “The MRM shall be based on an alternative methodology, set to capture on an equal basis, but adjusted to the specificities of the PRIIP, so as to assess the risk on a relevant basis.” compared to Categories I, II and III the risk of loss | 1 to 7 |
MRM methodology is specific to the category the fund is assigned to.

<table>
<thead>
<tr>
<th>Category II</th>
<th>Annualized Volatility</th>
<th>MRM Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Funds for which at least 2 years of historical daily prices or 4 years of historical weekly prices are available or where a natural benchmark or proxy can be identified to replace the missing period (relevant documentation on the benchmark/proxy is required)</td>
<td>&lt; 0.5%</td>
<td>1</td>
</tr>
<tr>
<td>• MRM class can range from 1 to 7 and is positively related to annualized volatility</td>
<td>0.5% - 5.0%</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>5% - 12%</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>12% - 20%</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>20% - 30%</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>30% - 80%</td>
<td>6</td>
</tr>
<tr>
<td></td>
<td>&gt; 80%</td>
<td>7</td>
</tr>
</tbody>
</table>

CRM is assessed at fund level only for those that face material counterparty risk or which must make predetermined payments to investors

“Materially” shall refer to a non-collateralized exposure on a counterparty, which shall account for 10% or more of the total assets/value of the fund

CRM is also assessed for funds at underlying investment level (look-through basis)

<table>
<thead>
<tr>
<th>Quality step</th>
<th>Credit Risk class</th>
<th>Rating Class</th>
<th>Impact on MRM</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>CR1</td>
<td>AA / AAA</td>
<td>None</td>
</tr>
<tr>
<td>1</td>
<td>CR1</td>
<td>AA</td>
<td>None</td>
</tr>
<tr>
<td>2</td>
<td>CR2</td>
<td>A</td>
<td>None</td>
</tr>
<tr>
<td>3</td>
<td>CR3</td>
<td>BBB</td>
<td>Floored at 3</td>
</tr>
<tr>
<td>4</td>
<td>CR4</td>
<td>BB</td>
<td>Floored at 5</td>
</tr>
<tr>
<td>5</td>
<td>CR5</td>
<td>B</td>
<td>Floored at 5</td>
</tr>
<tr>
<td>6</td>
<td>CR6</td>
<td>CCC</td>
<td>Floored at 6</td>
</tr>
</tbody>
</table>
Zoom on the SRI – Structured Products
What are we talking about

1. Complex SRI
   - Worst-of autocallable
   - Reverse convertible
   - Collared floater on CMS
   - Phoenix structured note
   - Cliquet structured note
   - CMS
   - Snowball
   - TwinWin certificates
   - Credit linked note
   - Etc.

2. Simple Derivatives
   - Turbo warrant
   - Index warrant
   - Warrant capped on indices
   - Etc.

Derivatives: MRM = 7 by default (no calculation, no change), simple payoff

Products could be then classified per level of complexity related to SRI or Performance scenario calculation

- **Simple**: derivatives/warrants, linear payoff, delta one
- **Medium**: capital guaranteed structured products, algo-based payoff
- **Complex**: others

Uncertainty around products in terms of actual complexity…
Synthetic Risk Indicator (SRI)
Credit Risk Measure (CRM)

For which PRIIPs?

Credit risk shall be assessed when the return of the investment depends on the creditworthiness of the manufacturer or party bound to make the relevant payment to the investor, directly or indirectly.

On most cases, credit risk shall be assessed on a look-through basis.

Where an entity directly engages to make a payment to the investor, credit risk shall be assessed for the entity that is the direct obligor. If the PRIIP or a financial product is packaged into another PRIIP, it needs also to be assessed together with the latter PRIIP.

A PRIIP which provides investors payoff linked to the performance or to the realisation of price changes or other conditions of financial assets.

A PRIIP entering into a financial derivatives or an efficient portfolio management, materially exposing the retail investor to the credit risk of such counterparty. Materially shall refers to a non-collateralised exposure on a counterparty.

A PRIIP investing in underlying PRIIPs or other investment instruments with a similar payment obligation or mechanism. The credit risk shall be assessed in relation to both the PRIIP itself and the underlying investment(s).
Zoom on the SRI – CRM
Methodology to assess Credit Risk

- PRIIPs will be assigned to **CRM classes 1 to 6**

### Details on CRM calculation:

1. **Determining the level of credit risk:**
   - ECAI (external credit assessment institution) assign credit assessment for the PRIIP
   - ECAI assign credit assessment for relevant obligor
   - Prescribed methodology for credit assessment in the RTS

2. Credit risk will be mapped into credit quality steps according to the **Directive 2009/138/EC.8**

3. Credit step adjusted depending on the credit risk mitigating or escalating factors and adjusted to reflect the maturity or the recommended holding period

4. Credit quality steps mapped into CRM

#### Adjusted credit quality step, in the case where the maturity of the PRIIP, or its RHP when a PRIIP does not have a maturity, is:

<table>
<thead>
<tr>
<th>Original credit step quality</th>
<th>Up to one year</th>
<th>Between 1 year and 12 years</th>
<th>More than 12 years</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
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<tr>
<td>2</td>
<td>1</td>
<td>2</td>
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<td>6</td>
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<td>6</td>
</tr>
</tbody>
</table>

Adjustments for maturity

**CASCADE BASIS** - credit quality step is the weighted average of each relevant obligor

**LOOK-THROUGH BASIS** - credit step is the highest of all credit risk exposures separately assessed (per layer)
Zoom on the SRI – Structured Products
MRM calculation requires complex methodologies

- Structured products with conditional protection of capital or with more than 5-year maturity shall be assigned to **MRM Classes 1 to 7**
  **Examples:** Reverse Convertibles, Twin Win notes, Phoenix

- MRM calculation: 97.5% Value-at-Risk based on forward simulations of the PRIIP's performance at the end of the recommended holding period (RHP), calibrated on historical data.

### Details on MRM calculation:

1. **Minimum 10,000 historical simulations of PRIIP value at end of RHP based on five years of (ideally, daily but at least monthly) historical returns of underlying assets or pricing factors.**

2. **Specific adjustments depending on underlying asset type**
   - Adjusted by dividends coupons for equities / bonds, PCA for curves…

3. **The PRIIP value on the relevant payment date(s) is calculated and discounted back to the present day.**

4. **Conversion into a VaR-equivalent volatility**

\[ VEV = \sqrt{\frac{3.842 - 2\text{VaR}}{1.96}} \]

<table>
<thead>
<tr>
<th>MRM class</th>
<th>Annualised volatility</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>&lt; 0.5%</td>
</tr>
<tr>
<td>2</td>
<td>0.5% - 5.0%</td>
</tr>
<tr>
<td>3</td>
<td>5.0% - 12%</td>
</tr>
<tr>
<td>4</td>
<td>12% - 20%</td>
</tr>
<tr>
<td>5</td>
<td>20% - 30%</td>
</tr>
<tr>
<td>6</td>
<td>30% - 80%</td>
</tr>
<tr>
<td>7</td>
<td>&gt;80%</td>
</tr>
</tbody>
</table>

PRIIPs will be assigned a MRM class according this table.
Performance Scenarios

Three circumstances: unfavourable, moderate and favourable

1. Unfavourable Scenario
   - Highlights the features of the product and the economic conditions which could give rise to an unfavourable outcome for the retail investor

2. Moderate Scenario
   - Highlights the features of the product and the economic conditions which could give rise to a moderate outcome for the retail investor

3. Favourable Scenario
   - Highlights the features of the product and the economic conditions which could give rise to a favourable outcome for the retail investor

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Unfavourable</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average return</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Moderate</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average return</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Favourable</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average return</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- Fair, accurate, clear and not misleading presentation to enable the retail investor to understand possible outcomes under different market conditions
- Each scenario accompanied by a narrative text (indicating, where applicable, conditions for returns to retail investors or performance caps)
- Information presented at the Recommended holding period (and for two interim periods, unless the RHP is shorter than 3 years or 1 interim period, unless the RHP is shorter than 1 year)
- Information for unfavourable, moderate and favourable scenario is based on estimated value of the PRIIP at 10th, 50th and 90th percentile respectively
- Performance calculated net of total costs (included proper assumptions on performance fees)
- Consistency with the information in other KID sections (e.g. for future profit participation, assumptions coherent with the ones on the annual rates of return of the underlying assets)

• For insurance-based PRIIPs, the three scenarios shall be calculated considering that no payments resulting from insurance coverage occur during the holding period. Notwithstanding, an additional scenario shall be included for insurance-based investment products, presenting the return in case an insured event occurs.
• An additional scenario shall be also added to show significant downward impact features of the product whether they are not adequately covered within the three standard scenarios.
Performance Scenarios
How to determine the unfavourable, moderate and favourable scenarios?

The scenario values under different performance scenarios shall be calculated in a similar manner to the market risk measure, i.e. based on the distribution of historical returns. The scenarios shall be calculated for the recommended holding period.

- The unfavourable scenario shall be the value of the PRIIP at the 10th percentile.
- The moderate scenario shall be the value of the PRIIP at the 50th percentile.
- The favourable scenario shall be the value of the PRIIP at the 90th percentile.

Calculation of expected values for intermediate holding periods

- For PRIIPs with a recommended holding period between 1 and 3 years, performance shall be shown at 2 different holding periods: 1 year and at the end of the recommended holding period.
- For PRIIPs with a recommended holding period of 3 years or more, performance shall be shown at 3 holding periods: 1 year, half the recommended holding period rounded up to the nearest year, and the recommended holding period.
- For PRIIPs with a recommended holding period of 1 year or less, no performance scenarios for intermediate holding periods shall be shown.
Key Information Document
Format and presentation of the Cost section

Reduction In Yield (RIY)

- Based on “moderate” performance scenario, using the same holding periods as in the performance scenarios
- Includes one-off, recurring and incidental costs, direct & indirect transaction costs (all contained in a single figure - RIY) and, if relevant, exit penalties

<table>
<thead>
<tr>
<th>Cost Category</th>
<th>Impact on return (RIY) per year</th>
<th>If you cash in after (1) year</th>
<th>If you cash in after [recommend at the recommended holding period/2] holding period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Impact on return (RIY)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This table shows the impact on return per year

One-off costs
- Entry costs
- Exit costs

Portfolio transaction costs
- Insurance costs
- Other ongoing costs

Incidental costs
- Performance fees
- Carried interests

The impact of the costs you pay when entering your investment. This is the most you will pay, and you could pay less.

The impact of the costs already included in the price. This is the most you will pay, and you could pay less.

The impact of the costs of selling underlying investments for the product.

The impact of the amount you are paying to buy insurance protection.

The impact of insurance costs (the amount you are paying for insurance cover which exceeds the estimated value of insurance benefits).

The impact of the costs that we take each year for managing your investments.

The impact of the performance fee. We take these from your investment if the product outperforms its benchmark by a certain margin.

The impact of carried interests. We take these when the investment has performed better than XVG. (A payment of 0% of the final return will take place subsequently to the end of the investment.)
**PRIIP’s costs**

Full breakdown: direct/indirect, one-off/recurring, insurance, incidental

### One-off costs

<table>
<thead>
<tr>
<th>% Entry costs</th>
<th>% Exit costs</th>
<th>% Portfolio transaction costs per year</th>
<th>% Insurance costs</th>
<th>% Other ongoing cost</th>
<th>% Performance fees</th>
</tr>
</thead>
</table>

- **Impact of entry costs taken before investment (maximum payable amount)**
- **Impact of exit costs when exit the investment upon maturity**
- **Impact of recurring costs taken each year from the investment, based on last year costs (best estimate). Figures cover all recurring costs, including insurance costs, management costs, operating expenses and portfolio transaction costs**
- **Impact of average performance fees / carried interest**

### Recurring costs

- **RIY is the Summary Cost Indicator** and shall be calculated as the difference between two percentages:
  1. The annual internal rate of return related to gross payments made by the investor and the estimated payments to the investor during the RHP
  2. The annual internal rate of return for the respective cost-free scenario

### Incidental costs

- **Costs are strictly related to the product in point; other costs charged by advising/selling persons are not shown**
- **Message to display: “figures are partially based on data from the past and thus may change in the future”**

---

**Investment [€10,000]**

<table>
<thead>
<tr>
<th>Scenarios</th>
<th>If you cash in after [1] year</th>
<th>If you cash in after [recommend] [at the recommended holding period/2] holding period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total costs</td>
<td><img src="image_url" alt="Image" /></td>
<td><img src="image_url" alt="Image" /></td>
</tr>
<tr>
<td>Impact on return (RIY) per year</td>
<td><img src="image_url" alt="Image" /></td>
<td><img src="image_url" alt="Image" /></td>
</tr>
</tbody>
</table>
PRIIP’s costs – challenges

Calculations of specific types of costs

- Computation of costs in all layers (including costs incurred in the underlying PRIIPs)
- Valuation techniques dependent on product complexity
- Compliant with accounting standards
- Calculation of fair value of biometric risk premium
- Consistency with Solvency II requested
- New fund’s returns estimation
- Computation of the effects of changes in fees or terms at the share class level

Look-through approach

Implicit costs

Transaction costs for new PRIIPs

Costs of biometric risk premium

Treatment of anti-dilution mechanisms

Performance fees

- Estimation of portfolio turnover
- Asset class dependent methodology
- Consistency with the investment policy requested
- Calculation of swing pricing effect on transaction costs using complex methodology
- New fund’s returns estimation
- Computation of the effects of changes in fees or terms at the share class level
The difference between the price and the fair value of the product shall be estimated as an estimation of the total entry costs included in the price of the product. The KID of a structured product should enable retailers to identify the amount captured by the manufacturer and the amount that will be used to provide the return.

Following list of not-exhaustive entry costs and charges that shall be taken into account in the amount to be disclosed:

1. Sales Commissions
2. Structuring costs (market making costs, spreads or Settlement costs)
3. Hedging costs
4. Legal fees
5. Cost for capital guarantee
6. Implicit premium paid to issuer

The notion of reduction in yield (model comparable approach or market-to-market model) determines the fair value of the products.

Zoom on entry costs for structured products.
KID Annual update and other mandatory refreshes

Key requirements

• Annual update – every 12 months (after initial publication and thereafter 12 months after latest review)

• Trigger management: Maintain process to identify “material changes” in the KID information (investment policy, SRI or expected returns, costs…)

• Revision of the KID upon “trigger” detection (without undue delay)

• Web publication 5 BD after revision

• (Revision requirements not applicable if PRIIPs not available to retail investors)
Agenda

Setting the scene: PRIIPs summary

Key Information Document

Solutions ahead
Key PRIIPs challenges to overcome

3 major PRIIPs impacts

Implement PRIIPs by 1\textsuperscript{st} January 2017 - you will need to take many organizational and functional decisions in order to develop new PRIIPs capabilities.

Set up a process to efficiently and effectively share data between the asset managers and its clients subject to PRIIPs KID requirements.

Implement the necessary operational unit to produce and maintain ongoing compliance on KIDs from 1/1/2017 for your non UCITS funds distributed to the retail.


** Potential for delay. EFAMA formal request 01.02.16
With a few months before becoming effective, PRIIPs is a race against time. You will need a pragmatic yet compliant solution for meeting your regulatory requirements and business imperatives at a reasonable cost.

**Proposed project workstreams**

**Awareness / Regulatory**
- Awareness sessions
- SME Expertise acquisition

**Data and Technology**
- Identification of data required for PRIIPs computation per contract type
- Identification of data/calculation that can be outsourced
- Identification of the high level ownership of data (within the Insurer’s organisation)
- Comparison between available data (internal Insurer system) and PRIIPs needs:
  - Identification of data sources
  - Identification of data owner
  - Planning of the gap remediation process.
- Based on the Deloitte’s Operating model methodology
- Organization of operating model workshops and formalization of the TOM
- Integration of the KID production into the insurance contract’s lifecycle
- Validation of methodologies for dynamic data calculation and updates per contract type

**Operations**
- Business case definition
- Identification of:
  - Fix cost (e.g. setup)
  - Recurring cost (e.g. maintenance)
  - Licence fees
  - Outsourcing fees
- Project management / monitoring implementation timeline and milestones
- Resource coordination
- Provision of SMEs Business Analysts

**Ex. TOM Methodology**
- Customers
- Channels
- Products and Services
- Processes
- Data
- Organisation
- People
- Technology
- Location

Which customers?
Via which channels?
Offered which products and services?
Supported by which processes?
Requiring what information?
Organised in which way to deliver?
Requiring which resources and skills?
Using which enabling technologies?
In which locations?
Data challenge for insurers

High-level view of data exchange and calculations illustrating the requirements to be flexible

1. Which methodological options will you accept for applying the KID rules?
   - MRM Fund Mgr A=f1(Data Pack A)
   - MRM Fund Mgr B=f2(Data Pack B)
   - MRM Fund Mgr C=f3(Data Pack C)

2. Multiple templates data pack formats
   - Be prepared to receive/collect multiple data templates from your universe of fund managers.

3. Flexible calculation engine to accommodate multiple templates and multiple calculation scenarios
   - Be prepared to apply different formulas for the same indicator.

4. Final PRIIP terms are policy contract specific
   - You will require computing and man power to run all those calculations!

5. Published KIDs to be revised and republished in case of material change
   - You will require the adequate system with audit trails to monitor the re-publication triggers
Data challenge for asset managers

High-level view of data exchange and calculations illustrating the requirements to be flexible

Fund Mgr

Insurer Company A

Insurer Company B

Insurer Company C

Data Pack A

Data Pack B

Data Pack C

MRM Fund Mgr = f₁(Data Pack A)

MRM Fund Mgr = f₂(Data Pack B)

MRM Fund Mgr = f₃(Data Pack C)

ULIP

ULIP

ULIP

KID

KID

KID

ULIP

ULIP

ULIP

KID

KID

KID

Multiple templates data pack formats
Be prepared to be requested multiple data templates from your universe of insurers clients.
“Data To Do List” for calculating the Risk, Performance & Costs sections

### Analysis
- Model review
- Validation of methodologies
- Fund classification for MRM
- Definition and review of benchmark assignment methodology
- Review of risk and performance narratives

### Risk & Reward Analytics
- Calculation of MRM
- CRM assessment
- Weekly SRI monitoring
- Calculation of performance percentiles (10th, 50th, 90th) over different time horizons
- Weekly MRM, CRM & Performance monitoring

### Reduction in Yield
- Application of appropriate performance fee calculation methodology
- Factoring of management fees
- Calculation of Reduction in Yield

### Narratives
- Generation of narratives in line with draft RTS:
  - What is this product
  - Target Market
  - Risk and Performance scenarios
  - Liquidity
  - Costs
  - Reduction in Yield
  - Others
“Data To Do List” for generating PRIIP data packs (aka transparency reporting) to your insurance investors

**Activities**

- Review of each methodology available
- Cost/benefits analysis
- Identification and selection of benchmarks
- Assistance to implementation

**Analysis**

**Data management**

- Acquisition and maintenance of fund historical performance and dividends
- Acquisition and maintenance of risk metrics
- Integration of cost data
- Generation of narratives in line with draft RTS

**Analytics and calculation**

- SRI analytics:
  - Direct SRI calculation and conservative average,
  - Total return performance history,
  - Ex-post risk analytics
- Performance analytics:
  - Direct calculation of the performance scenarios

**Monitoring & Maintenance**

- Monitoring of major changes in the portfolios and subsequent update of the transparency data
- Monitoring of MRM/SRI
- Communication through a standardized [data exchange template](#)
Data Exchange Template

Overview

1. Input from Asset Managers (static data)
   - Scope, PRIIP classification, benchmark/proxies used, narratives

2. Input from Asset Servicers / Managers (dynamic data)
   - Costs, credit risk exposures, NAV time series, dividends, benchmark/proxies data, asset mix

3. Output to the Insurance Company (dynamic data)
   - Calculated risk, performance and costs data ready to be incorporated in the KID assembly
## Input of costs

<table>
<thead>
<tr>
<th>Field</th>
<th>Entry Cost</th>
<th>Exit Cost</th>
<th>Ongoing Fees</th>
<th>Performance Fees</th>
<th>Hurdle Rate</th>
<th>Transaction cost</th>
<th>Anti-dilution mechanisms</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Explanation</strong></td>
<td>Entry cost of a compartment *</td>
<td>Exit cost of a compartment *</td>
<td>Management fees, per annum *</td>
<td>Performance fees, per annum *</td>
<td>Minimum return for Performance fees *</td>
<td>Estimated annualised transaction costs mechanisms (excluding swing factors)</td>
<td>Indicates whether the PRIIP uses anti-dilution mechanisms</td>
</tr>
<tr>
<td><strong>Mandatory</strong></td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>

## Dynamic output

<table>
<thead>
<tr>
<th>Field</th>
<th>VaR</th>
<th>VEV</th>
<th>MRM</th>
<th>CRM</th>
<th>SRI</th>
<th>Liquidity</th>
<th>Quantile 10% (Net) 1Y</th>
<th>Quantile 10% (Net) 2Y</th>
<th>Quantile 10% (Net) 3Y</th>
<th>Quantile 10% (Net) 4Y</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Explanation</strong></td>
<td>Cornish-Fischer VaR at 97.5%</td>
<td>VaR Equivalent Volatility</td>
<td>Market Risk Measure</td>
<td>Number of weeks since MRM has changed</td>
<td>Credit Risk Measure</td>
<td>Summary Risk Indicator</td>
<td>Average Asset Liquidation Time</td>
<td>Average Asset Liquidation Time - stressed conditions</td>
<td>Net performance for the unfavourable scenario</td>
<td>Net performance for the unfavourable scenario</td>
</tr>
<tr>
<td><strong>Risk MRM</strong></td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>

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**Link’n Learn 2016 - PRIIPs**
How we can help?
We can help getting you up to speed and setting you up with PRIIPs this year and help you get the information you need to satisfy both your clients and the regulators.

The devil is in the details. With the introduction of PRIIPs KIDs on 1 January 2017, the insurance industry faces a new reporting challenge. Deloitte is committed to help you face that challenge by providing you with the necessary experts to identify what is left to be done, what information and calculations are required, how to retrieve those, what this means for your systems and interfaces. We can help you managing the impacts on your internal organization, on the way you do business is impacted, on the way to manage your products, your providers and your clients. Finally we can help you making it work altogether.

Producing a KID will require a lot of information from the fund manufacturers (internal or external): the data necessary to calculate the risk measures, but other data elements such as future performance data, costs, “target market”, “risk narratives”.

With hundreds of funds (if not thousands) being available to insurance clients, given the absence of data exchange norms, one should prepare for a situation where insurers will need to cope with many different PRIIPs data packs from fund managers and process them, or find alternative solutions when information is not available.

Deloitte will assist its clients to define the required information in light of their specific business model, will assist in sourcing and collecting it, will perform the necessary calculations and enrichment to allow for a smooth KID production process.

Deloitte’s PRIIPs KID factory is today able to produce and maintain “live” documents based on the level of information known today. It leverages the experience in terms of processes, data management, technological developments accumulated with the current KIID factory that produces approx. 300,000 on a yearly basis.

| Assembly | Document Management | Document Availability | Web Maintenance |

- 130,000 calculations on an annual basis
- 300,000 UCITs KIIDs generated on an annual basis
- 2,500,000 UCITs KIIDs downloaded monthly from our platform

UCITS KID experience

Link’n Learn 2016 - PRIIPs
Our risk platform leverages and enriches your data to meet these challenges

Our main differentiating factors

- **Interfaced with main Fund Administrators**
  - Key accelerator for on-boarding phases
  - No golden source: use of proprietary data interfacing ETL
- **Validation of calculation methodologies and narratives with our regulatory experts**
  - Experienced team of risk, derivatives and IT specialists
  - Regulatory client support
- **Flexible reporting solutions**
  - Weekly/monthly reporting
  - Reporting at portfolio or share-class level
  - Email or SFTP delivery
- **Proven platform with a long-term track record**
  - Extensive experience from UCITS KIDs and funds factsheet factory, covering 2,000+ share classes
  - Large scale institutional reporting factory, covering 1,000+ portfolios

Link’n Learn 2016 - PRIIPs
Please join us on the 12th May for our next webinar in the series: Derivative Financial Instruments - Introduction to Valuation with Guillaume Ledure, Herve Hens & Stefano Portolan
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