



PRIPs - Transitioning To Implementation



5 May 2017

KPMG Insurance Ireland Strategic Alliance Partnership

#PRIIPs

Welcome & Introduction

Brian Morrissey

Partner & Head of Insurance, KPMG

KPMG/Insurance Ireland Strategic Partnership

- **Insurance Ireland and KPMG have a Strategic Alliance Partnership on Conduct and the Customer. This Partnership considers existing and proposed regulation to deliver better regulatory outcomes for the consumer, the industry and the regulator.**
- **The SAP is looking at regulatory implementation projects firms will be required to undertake and how to approach them. It will also consider the learning points to be taken from the PRIIPs process to see how best to inform the regulatory process for future EU legislation.**
- **A series of industry briefings are being held throughout 2017 with KPMG's Centre of Excellence to inform the industry's response to developments in this area.**



Kevin Thompson
CEO, Insurance Ireland



Niamh Mulholland
Associate Director, Regulatory, KPMG



PRIIPS & the Lamfalussy Process for EU Regulation

PRIPs: Introduction

Why Regulate at EU Level?

- **Uniform Rules on Transparency:** Improving provisions on transparency of PRIIPs offered to retail investors is an important *investor protection measure* and a *precondition for rebuilding confidence of retail investors in the financial market*, in particular in the aftermath of the financial crisis.
- **National Regulation:** Member States had taken divergent and uncoordinated action to address shortcomings in investor protection and this was considered to both distort competition and creates an obstacle to the smooth functioning of the internal market.
- **Level Playing Field:** In common with other key pieces of European Financial Services Legislation, it was felt that a European Regulation in this area was necessary to address the un-level playing field between different products and distribution channels that had emerged as a result of the existence of different rules on PRIIPs, that varied according to the industry offering, the PRIIPs themselves and differences in national regulation in this area.
- **Taking the lead from UCITS:** the first steps in this direction had already been taken at Union level through the development of the key investor information regime (*UCITS KIID*) established in Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities.

PRIPs: Introduction

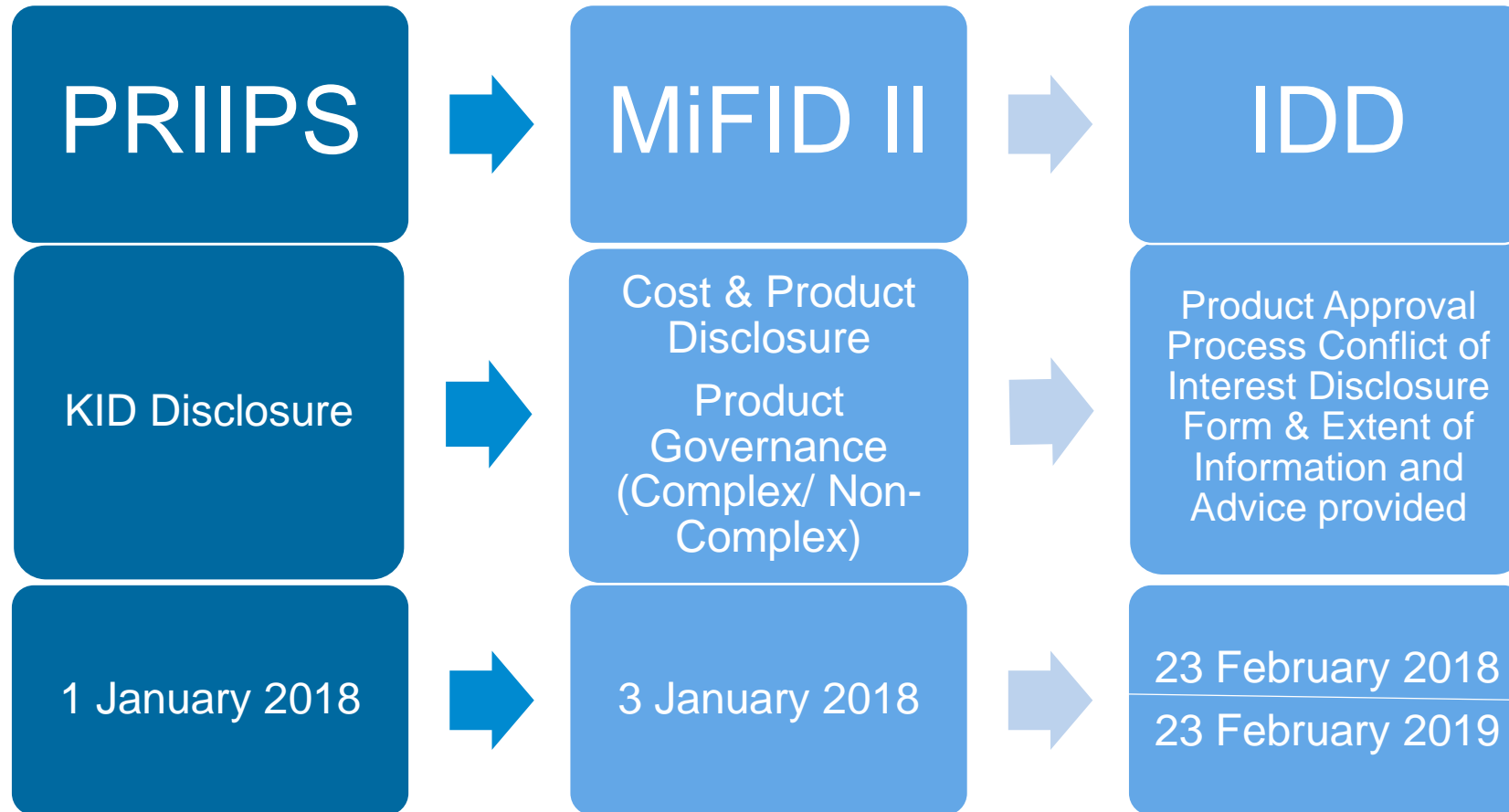
Case Study in Lamfalussy

Level 1	Directive <ul style="list-style-type: none">■ Not directly applicable■ Requires Member State transposition	Regulation <ul style="list-style-type: none">■ Directly applicable■ Limited Member State transposition
Level 2	Delegated/implementing acts (regulations or directives): <ul style="list-style-type: none">■ Drafted and adopted by Commission following advice from ESA Regulatory/implementing technical standards (regulations): <ul style="list-style-type: none">■ Drafted by ESA and adopted by the Commission	
Level 3	ESA guidelines and ESA/Commission FAQs to achieve consistent implementation in Member States	
	National implementation (not strictly Level 3): <ul style="list-style-type: none">■ Primary or secondary legislation, regulatory rules■ Penalty regimes	
Level 4	Enforcement <ul style="list-style-type: none">■ Commission verifies Member State compliance with EU law■ Commission legal action against Member States suspected of breaches of EU law■ National competent authorities monitoring compliance with rules by regulated firms	



Insights into the Regulatory Process?

Timeline 2016 - 2019 - Broader Regulatory Context





PRIIPs: What We Know

PRIPs: Background & Objectives

Purpose

- Seeks to promote investor protection by enhancing transparency over the key features and risks of PRIIPs sold to retail investors

Scope

- Definition is broad in nature and includes Retail AIFs, UCITS Funds (from 2020), Retail structured products, derivatives and life assurance based investment

Sectors

- Fund managers, insurance undertakings, credit institutions and investment firms will need to assess the impact of PRIIPs to their product/ service offering and business models

PRIIPS: Overview of Requirements

- **Applies to persons who (a) manufacture PRIIPs or (b) advise on or sell PRIIPs**
- **PRIIPS proposes the introduction of the Key Information Document (KID) when investment products are sold to retail consumers.**
- **The principle behind the KID is that consumers should have access to information that is easy to understand and facilitates straightforward comparison between investment products. The objective of the KID is that consumers' engagement with investment products will be improved.**
- **The production of the KID represents a challenge for both firms and regulators, due to the range and diversity of investment products, ensuring that the KID is fit for purpose and achieves the objectives intended.**
- **PRIIPS requires:**
 - a common mandatory 3-page template for the KID;
 - a summary risk indicator of seven classes for the risk and reward section of the KID;
 - a methodology to assign each PRIIP to one of the seven classes contained in the summary risk indicator, and for the inclusion of additional warnings and narrative explanations for certain PRIIPs;
 - details on forward performance scenarios and a format for their presentation, including possible performance for different time periods and at least three scenarios;
 - costs presentation, including the figures that must be calculated and the format to be used for these i.e. in both cash and percentage terms;
 - rules on revision and republication of the KID, to be done at least each year; and the ability to identify a target market.

PRIIPs: What is a KID?



Forward looking document unlike UCITS KIID



Stand-alone document separate from marketing material



Maximum 3 A4 pages



A comprehension alert where applicable (aligned with MiFID II)

Key Information Document	
Purpose	This document provides you with key information about this investment product. It is not marketing material. The information is required by law to help you understand the nature, risks, costs, potential gains and losses of this product and to help you compare it with other products. <i>(When relevant, applicable) You are about to purchase a product that is not simple and may be difficult to understand.</i>
Product	[Name of Product] [Name of PRIIP manufacturer] (where applicable ISIN) (website for PRIIP manufacturer) (Call (telephone number) for more information) (Competent Authority of the PRIIP Manufacturer in relation to the PRIIP) (date of production of the KID)
What is this product?	Type Objectives Intended retail investor
Insurance benefits	What are the risks and what could I get in return?
Risk Indicator	Description of the risk-reward profile Summary risk indicator SRI template and narrative as set out in Annex III or possible maximum loss, can I lose all invested capital? Do I bear the risk of incurring additional financial commitments or obligations in their capital production against market risk?
Performance Scenario	Performance Scenario template and narrative as set out in Annex V including where applicable information on conditions for returns to retail investors or best-in performance caps, and statement that the tax legislation of the retail investor's home Member State may have an impact on actual period.
	What happens if [PRIIP Manufacturer] is unable to pay out? Information on whether there is a guarantee scheme, the name of the guarantor or investor compensation scheme operator, including the risks covered and those not covered.
	What are the costs? Costs over time Template and narrative according to Annex VII
	Composition of Costs Template and narrative according to Annex VII Narrative on information to be included on other distribution costs
	How long should I hold it and can I take money out early? Recommended (required minimum) holding period: (x) Information on whether one can disinvest before maturity, the conditions on this, and applicable fees and conditions if any. Information on the consequences of cashing in before the end of the term or before the end of the recommended holding period.
	How can I complain?
	Other relevant information



Accurate, fair, clear and not misleading



Written in the language of the country where it is distributed



Provided in good time before the retail investor is bound by any contract



Regularly reviewed by the manufacturer

PRIIPS: Addressing the key requirements for the KID

Other relevant information

- Any additional information documents
- May be provided in summary format, including a link to the website where further details to documents are made available

How can I complain?

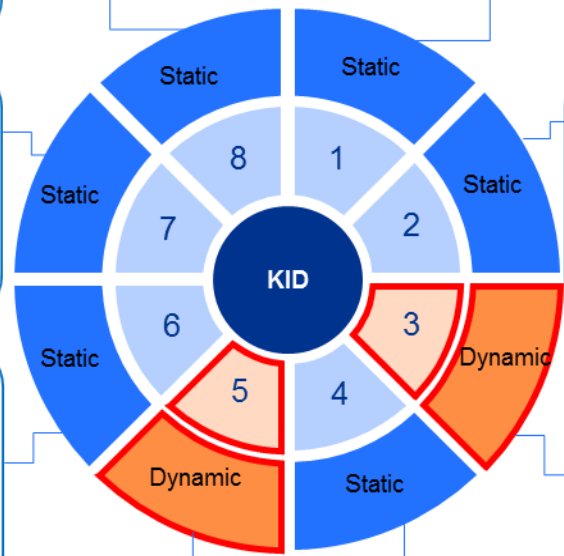
- steps to be followed for lodging a complaint about the product or the conduct of the PRIIP manufacturer or the person advising on, or selling, the product
- A link to the relevant website for such complaints
- An up-to-date postal address and an email to which such complaints may be submitted

How long should I hold it and can I take my money out early?

- a brief description of the reasons for the selection of the recommended holding period and, where present, the required minimum holding period
- a description of the features of the disinvestment procedure and when disinvestment is possible
- information about any fees and penalties which are incurred for disinvestments prior to maturity, including a cross reference to the information on costs

What are the costs?

- the methodology has been set out
- the 'Costs over time' table – to specify the summary cost indicator of the total aggregated costs in monetary and percentage terms
- the 'Composition of costs' table – to specify any one-off costs, recurring costs, relevant incidental costs in percentage terms



General information

- the name of the PRIIP assigned by the PRIIP manufacturer and, where present, the PRIIP's ISIN or Unique Product Identifier
- the legal name of the PRIIP manufacturer
- the PRIIP manufacturer's specific website address and a phone number
- the name of the NCA
- either the date of production or the date of the latest revision of the key information document

What is this product?

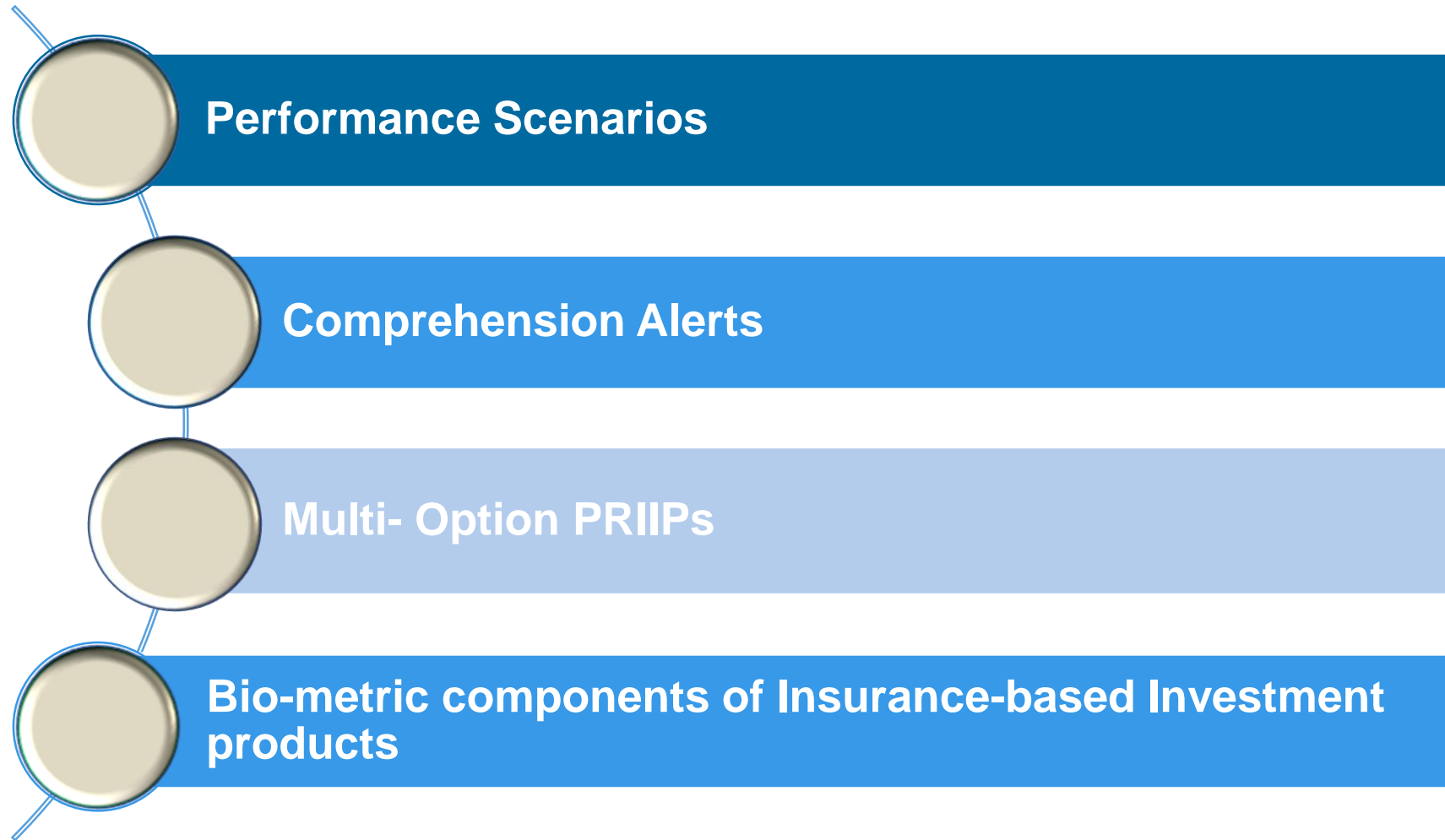
- the main factors upon which return depends, the underlying investment assets or reference values, and how the return is determined, and the relationship between the PRIIP's return and that of the underlying investment assets or reference values.
- the target retail investors identified by the PRIIP manufacturer
- the details of insurance benefits
- the maturity date, circumstances when the PRIIP can be terminated

What happens if [company] is unable to pay out?

- the methodology has been set out
- the level of risk** – using a summary risk indicator with a narrative (e.g. when a PRIIP is denominated in a foreign currency)
- four performance scenarios**
- pay-off structure graphs for ETDs

What happens if [company] is unable to pay out?

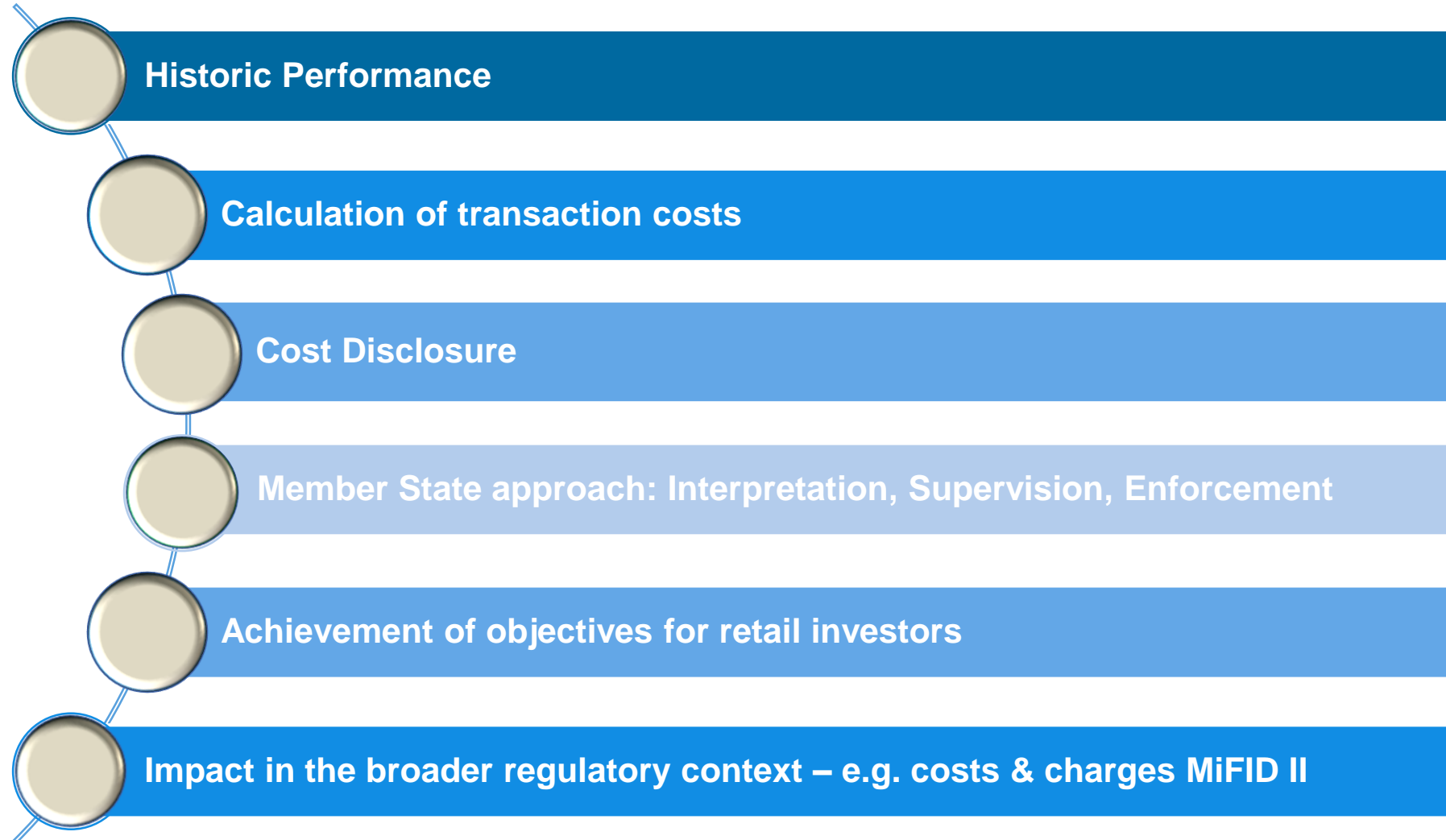
PRIIPs Delegated Regulation: Key Clarifications





PRIIPs: Remaining Questions

PRIIPs Delegated Regulation: Remaining Questions





John O'Donnell

Head of Insurance Risk and Regulatory, KPMG

Agenda

- **Usefulness, Opportunity or Compliance Cost**
- **KID Content**
- **Product design and KID Production Considerations**
- **The link to Personal Illustrations**
- **Governance**

PRIIPs - Usefulness, Opportunity or Compliance Cost

- Rules based regulation?
- Help build consumer confidence?
- Transparency, Simplification?
- Useful for comparison purposes ✓
- Risk Indicator – correlation with reward?

← Limitations

→ Product design opportunities



KID Content

Summary Risk Indicator

CRM class \ MRM class	MR1	MR2	MR3	MR4	MR5	MR6	MR7
CR1	1	2	3	4	5	6	7
CR2	1	2	3	4	5	6	7
CR3	3	3	3	4	5	6	7
CR4	5	5	5	5	5	6	7
CR5	5	5	5	5	5	6	7
CR6	6	6	6	6	6	6	7



- ❑ SRI indicator is a **combination** between **market risk and credit risk**.
- ❑ To derive required market risk computation methodology, **investment products need to be classified**:
 - Cat 1: Investor can loose more than the money invested; products for which pricing frequency is less than monthly or valuation history (incl. proxy) not available.
 - Cat 2: Fixed leverage product with history (daily: 2 years; weekly: 4 years; monthly: 5 years).
 - Cat 3: Variable pay-off products with history.
 - Cat 4: Products value depends in part on factors not observed in market.
- ❑ Investment products in category 1 will be automatically classified while other categories will require the computation of VaR Cornish-Fischer (Cat 2) or VaR Bootstrapping (Cat 3 and 4) to determine market risk measure.
- ❑ Credit risk is a combination between the creditworthiness of the product manufacturer (not applicable to investment funds) and the ones of underlying investments (if > 10% product exposure and not collateralized).
- ❑ Product manufacturers will be required **to look through their portfolio and assess credit risk** based on underlying issuer ratings.

Projected performance scenarios

Investment Insurance premium

		1 year	[3] years	[5] years (Recommended holding period)
[Survival] Scenarios				
Stress scenario	What you might get back after costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
	Average return each year	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Unfavourable scenario	What you might get back after costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
	Average return each year	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Moderate scenario	What you might get back after costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
	Average return each year	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Favourable scenario	What you might get back after costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
	Average return each year	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

[Death] Scenario

[Insured event]	What your beneficiaries might get back after costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
------------------------	-----------------------------------------------------------	--------------------------	--------------------------	--------------------------

- Performance scenario is a **simulation of future investment product's performances**.
- Investment product's holding period should be considered to select performances time horizon
- Simulation principles are the same as the ones for SRI market risk measures computation with a **quantile approach**:
 - 10% for unfavourable.
 - 50% for moderate.
 - 90% for favourable.
 - Stressed simulation varies depending on product category.
- Performance scenarios should be **disclosed net of costs** which is requiring the netting of cost items from required KID cost table.
- In the case of **performance fees**, Product Manufacturers should simulate **proxy(ies) future performances and compute forward looking performance fees** to be deducted from investment product's gross performance.

Overview of cost requirements

- ❑ **As part of the “costs” section of the PRIIP KID should be disclosed the following tables:**
 - “Composition of costs” which should specify, in % terms and based on historical data, any one-off costs (entry/exit charges), ongoing costs and incidental costs (such as perf. fees & carried interests).
 - “Cost over time” which should specify, in monetary and % terms, the forward looking summary cost indicator (total aggregated costs) of the PRIIP, based on required time horizon.
- ❑ **Main change since UCITS is the requirement to include transaction costs as part of the ongoing costs item of the “composition of costs” table.**
- ❑ **Transaction costs should be annualized based on 3 years transaction history where transaction cost is understood as the difference between the “arrival price” (mid price) when the order is transmitted for execution and the net realized execution price.**
- ❑ **Should 3 years transaction history not be available, transaction costs should be assessed based on estimated portfolio turnover per sub-asset type and related unit transaction cost derived from proxies (average bid-ask spread divided by 2).**
- ❑ **Transaction costs for “illiquid” assets shall be calculated based on fair value methodology.**

Costs over time - Reduction in Yield (RIY)			
Investment [€10 000]			
Scenarios	If you cash in after [1] year	If you cash in after [recommend end of the recommending period/2]	If you cash in [at the end of the holding period]
Total costs	€	€	€
Impact on return (RIY) per year	[%]	[%]	[%]

Full Disclosure of Costs

This table shows the impact on return per year			
One-off costs	Entry costs	[]%	The impact of the costs you pay when entering your investment. [This is the most you will pay, and you could pay less]. [AND/OR where the costs are embedded in the price, for instance in the case of PRIPs other than investment funds] The impact of the costs already included in the price. [This is the most you will pay, and you could pay less]. [Where distribution costs are included in entry costs] This includes the costs of distribution of your product.
	Exit costs	[]%	The impact of the costs of exiting your investment when it matures.
Ongoing costs	Portfolio transaction costs	[]%	The impact of the costs of us buying and selling underlying investments for the product.
	Other ongoing costs	[]%	The impact of the costs that we take each year for managing your investments and the costs presented in Section II.
Incidental costs	Performance fees	[]%	The impact of the performance fee. We take these from your investment if the product outperforms its benchmark [y by x%].
	Carried interests	[]%	The impact of carried interests. We take these when the investment has [performed better than x%]. [A payment of y% of the final return will take place subsequently to the exit of the investment.]



Product Design and KID Production

Product design considerations

- Level Playing Field
- Recommended Holding Period v Churn
- Costs - Reduction in Yield v Competitors
- Diluted effect of teasers and other marketing methods
- Performance / fees - Upside Reward v Downside Pain
- Risk mitigation again risks of civil liability

KID Production – Initial Considerations

- In-house / Outsourced
- Point in time only / On demand
- Approach to Multi-Option PRIIPs
- European PRIIPs template
- Funds of Funds
- Revisions, Translations

Volume and Sources of Data

KID Production – Operational and Strategic issues

- Short timescales 1/1/2018– and then ongoing
- Extent of external dependencies
- Dataset – deep asset manager data now available (advantages?)
- Manager selection and evaluation – due diligence
- Computational complexity (validation?)
- Where will market focus - SRI / performance scenarios / costs



Personal Illustrations

PRIIPS KIDs and other Illustrations

- General Information (KID) v Personalised (Illustrations)
- Requirement not to contradict KID – Is the use of different bases acceptable?
- Ireland – CBI - Alignment with or replacement of Life Disclosure Regulations
- UK FCA Position (CP16/18)
- Effective Supervision better than narrow rules



Governance

Governance issues

- Target market
- Interaction with IDD (product oversight and governance) and MiFID II
- Ensuring accuracy of disclosures
- Inventory of PRIIPs and related KIDs
- Consistency with contractual documents
- Training of Distributors and in-house functions



Questions and Answers



Thank you



kpmg.ie

© 2017 KPMG, an Irish partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. Printed in Ireland.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

The KPMG name and logo are registered trademarks of KPMG International Cooperative (“KPMG International”), a Swiss entity.