KIDS for PRIIPS – a guide for Chief Actuaries

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Agenda

• Background Information
• What does the KID need to include?
• How are the figures calculated?
• Monitoring compliance
• Biggest implementation challenges
• Q&A
Regulatory background

New EU-wide disclosure requirements from 1 January 2018
Key Information Documents (KIDs) required for Packaged Retail and Insurance-Based Investment Products (PRIIPs)
Standardised, non-personalised point of sale document
Aim is to help retail investors better understand product and risks before investing

NOT A MARKETING DOCUMENT

What products are captured?

- Collective investment schemes
- Investment trusts
- Unit-linked and with-profits savings products
- Holloway products
- Pensions contracts
What does the KID need to cover?

• 3 page point of sale document
• Prescribed structure
• Some prescribed wording

• Demo of a KID document
### What needs calculating?

#### Risk Indicators

#### Performance Scenarios

#### Impact of costs on return achieved

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**Summary Risk Indicator**

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<tr>
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<th>MR1</th>
<th>MR2</th>
<th>MR3</th>
<th>MR4</th>
<th>MR5</th>
<th>MR6</th>
<th>MR7</th>
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</table>
Categorisation

• How to calculate Market Risk Measure and Performance Scenarios depends on category of PRIIP
• Most insurance products will fall into Categories 2-4

<table>
<thead>
<tr>
<th>Category</th>
<th>Key features*</th>
<th>Examples</th>
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<tbody>
<tr>
<td>2</td>
<td>“offers non-leveraged exposure to the prices of underlying investments”</td>
<td>Unit-linked</td>
</tr>
<tr>
<td>3</td>
<td>“values reflect prices of the underlying investments but not as a constant multiple”</td>
<td>UL with guarantee or Investment Trust</td>
</tr>
<tr>
<td>4</td>
<td>“values depend in part on factors not observed in the market”</td>
<td>With-Profits</td>
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Calculation Methodologies

• Methodology for Market Risk Measure and Performance Scenarios
  – Closed-form Formula for Category 2
  – “Boot-strapping” projections for Category 3

• Assumptions
  – Historic returns adjusted to risk-free expected return for MRM
  – Historic returns allowing for costs for Scenarios

Calculation Outputs

<table>
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<th>Calculation</th>
<th>Confidence Level</th>
<th>Assumptions</th>
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<tbody>
<tr>
<td>Market Risk Measure</td>
<td>97.5%</td>
<td>Historic Returns adjusted to risk-free</td>
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<tr>
<td>Favourable Scenario</td>
<td>10%</td>
<td>Historic Returns allowing for costs</td>
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<tr>
<td>Moderate Scenario</td>
<td>50%</td>
<td>Historic Returns allowing for costs</td>
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<tr>
<td>Unfavourable Scenario</td>
<td>90%</td>
<td>Historic Returns allowing for costs</td>
</tr>
<tr>
<td>Stress Scenario</td>
<td>95% (for holding periods &gt;1y)</td>
<td>Adjusted Historic Returns allowing for costs</td>
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</table>
Why are calculations non-trivial?

Modelling non-market features

• For Category 4 PRIIPS, separate out “market” and “non-market” features
• Model “market” features as Category 2 or 3 as appropriate
• Non-market features shall follow “robust and well-recognised industry standards for determining expectations and levels of uncertainty of the contribution”
  – Use an asset share approach for smoothing etc
Impact of costs

• Methodology akin to that used for existing Key Features Illustrations
  – Reduction in yield calculation
  – Greater granularity needed

• Transaction Costs
  – May need to obtain from investment manager

Examples of challenges

• Modelling payouts if not targeting Asset Share
• Smoothing
• Share price vs NAV for Investment Trusts
• Monthly vs Daily Data
• Changed Investment Strategy
• Changed Investment Manager
• Multiple option products / systemisation

If we get it wrong, FCA has wide range of powers!
When does a KID need updating?

12 months have passed since previous KID

SRI changes (monitored over a 4 month period)

Mean return in performance scenario changes by more than 5%

BW view: Requires monthly monitoring

Conclusions

• Calculations are not particularly difficult but probably beyond the “marketing team”

• Some areas are likely to need a bit of up-front work SOON
  – Historic Investment Return data
  – Asset Share Methodology for With-Profits
  – Expense and Costs Information
  – Systemisation and version control / records

For more details or to have a 1-1 discussion of your needs please contact: scott.eason@barnett-waddingham.co.uk
Q&A

Regulatory Information

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