A Deeper Dive Into The “Final Draft” RTS For PRIIPs KIDs

Delving more deeply into the details of the latest PRIIPs KIDs regulatory technical standards (RTS) shows that there are, after all, some important differences from the previously published version.

It was reported that some members of the Economic and Monetary Affairs Committee (ECON) had expressed concern that allowing manager discretion on performance scenarios could create over-optimistic scenarios, so that discretion has been all but removed –

- The unfavourable, moderate and favourable return scenarios “shall be calculated in a similar manner to the market risk measure”, i.e., for funds at least, future returns based on up to five years of historical prices. The moderate scenario is to be the median “expected” return at the recommended holding period (RHP) based on given formulae, with similarly prescribed values for the favourable and unfavourable scenarios;
- The unspecified “alternative methodology” suggested for the market risk measure (MRM) of Category 4 PRIIPs (With Profits) is now set down as a combination of ‘bootstrapping’ simulation, historical data and “robust and well recognised industry and regulatory standards for determining relevant expectations”;
- PRIIPs will be divided into 4 categories rather than 5 as there is no longer a category for PRIIPs investing in illiquid assets or with insufficient data histories;
- While there was previously no indication of what would constitute a material change leading to the review of a KID, we now know that this must be done at least if the “mean return for the PRIIP’s moderate performance scenario, expressed as an annualised percentage return, has changed by more than five percentage points”;
- The previous draft RTS said return scenarios would need to be shown for the RHP and two interim periods. These interim periods have now been prescribed:
    - PRIIPs with a RHP of 1 year or less: no interim term,
    - PRIIPs with an RHP of 1-3 years, an interim term of 1 year, and
    - PRIIPs with an RHP of >3 years, interim terms of 1 year and half the RHP.

The bands between the different levels of the MRM have been widened enormously, removing consistency with the SRRI bands on UCITS KIIDs (MRM 7 is now annualised volatility of >80% instead of >25%).

The Credit Risk Measure (CRM) is based on a product life of 1 to 12 years, with minor adjustments down for shorter-term products or up for products with a life of over 12 years. While the table that combines the MRM and CRM to give us the final SRI has not changed, the widening of the bands means that fewer PRIIPs are likely to have an MRM of 6 or 7, so any credit risk could still make a difference to the overall SRI.

The different investment amounts to be used for cost and return illustrations have been streamlined, with 10,000 euros (or other currency) used for all lump sums and 1,000 p.a. for regular savings insurance products. A new template has been introduced in the form of a graph to show the possible returns for exchange traded futures and options, alongside the tables for other lump sum and regular savings PRIIPs.

As before, the section on the calculation of costs is long and detailed to make sure every cost in every eventuality for every product type is included and there is no room for doubt. What has changed, though, is the "costs over time" table, which has been simplified to remove the individual elements that make up the total costs. It now consists of only two lines – total monetary values and Reduction In Yield percentage – for each of the prescribed timescales.

Where previously there was no obligation for PRIIP manufacturers to inform existing clients of changes to the KIDs, the RTS now requires that, "where it is possible and the PRIIP manufacturer has access to the details of retail investors, the PRIIP manufacturer should inform the retail investors when the key investor documents have been revised, for example by means of mailing lists or email alerts". This is unlikely to affect fund groups whose retail customers come through aggregators or those whose KIDs tend not to need updating more than once a year. But it could affect life companies who hold details of individual clients and investment trust companies with registers full of retail investors. We expect annual/interim reports – and maybe even monthly factsheets – will include a statement directing clients to the latest KID on the website.

What is still not clear is how much text, if any, is prescribed and how much is indicative. There are many places in the RTS where the text is shown in square brackets, implying it is open to PRIIPs manufacturers to insert their own text, from which the implication could also be that the text shown without square brackets is non-negotiable. The emphasis on plain language remains, at least in the "What is this product?" and SRI narrative sections, where specific reference is made to it. We also know that the avoidance of jargon and technical terms is a fundamental requirement if a PRIIP is to achieve its goal and meet investor needs. All in all, the internal and external cross-references, coupled with some lengthy product definitions, don't make for an easy read, but we will be happy to share our interpretation of the requirements with interested parties.

If you require further information please get in touch with us by calling 020 7337 2291 or by email at fe-kiihub@financialexpress.net.

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