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Key Information Document for retail investors

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Important Disclaimer!

This presentation should not be intended or reported as expressing the views or the policy of CESR or ESMA.

The views expressed in this material represent exclusively those of the author

Contents

1. Background

Background (1)

1. Protection of consumers is a constitutional-rank pan-European principle (Art. 12, TFEU; ex Art. 153(2), TEC)

2. In order to pursue their financial objectives individuals should be able to make informed decisions on investments opportunities

3. Financial markets, services and products present several features that are not easily comprehensible by the average retail investor

- Public policy must intervene to ensure that information provided to retail investors is meaningful, complete and easily comprehensible

- Harmonization in the Single Market: information on investment opportunities in the (UCITS) market must be consistent and comparable for the benefit of all stakeholders, no regulatory arbitrage!

Background (2)

The UCITS III Directive (85/611/EEC) already provided, in addition to the Full Prospectus of the fund, for a more concise and simple instrument of pre-contractual information of investors: the Simplified Prospectus - SP (Articles 27 to 33 and Schedule C of Annex I of Directive 85/611/EC).

The European Commission had issued a Recommendation (2004/384/EC) on the SP, to provide guidance on some crucial elements of the document and improve harmonization in the supervisory practice across the EU.

…however...

- Directive 85/611/EEC set out only rather general requirements on the SP (minimum harmonization, no Lamfalussy process applied);

- the EC Recommendation does not impose legally binding rules.

as a result, the review of some years after has shown how some of the objectives of the SP had not been fully achieved…

Background (3)

Recommandation	N. MS	% Tot.
Objective	21	84%
Joint Pres. Objective and Inv. Policy	20	80%
TaxRegime	20	80%
Investm. Policy	19	76%
Expected Cost Structure	19	76%
Risk Profile	18	72%
UCITS' Historical Performance	16	64%
Specific Risk	15	60%
Entry and Exit and Other Fees	15	60%
Prioritisation of info. Disclosure	14	56%
TER	14	56%
Costs not included in the TER	14	56%
Turnover Rate	14	56%
Cumulative Performance	13	52%
Exclusion of Subscription and Redemption fee	13	52%
Identify and Classify Fee Sharing Agreements	13	52%
Identify Soft Comm.	13	52%
Presence of Fee Sharing Agreements and Soft Comm.	12	48%
Reference to Full Prospectus	12	48%
Benefit of Fee-Arrangements	11	44%
Presentation of TER and Turnover	9	36%
Synthetic risk indicator	5	20%
Disclosure of Benchmark	3	12%

Insufficient harmonization

2. The policy and legislative process

The policy and legislative process (1)

Legislative context

- The UCITS IV Directive (2009/65/EC) was adopted on 13 July 2009 (repealing Directive 85/611/EEC)

    - Article 78 – Key Investor Information (KII) replaces SP for UCITS

- ✓ Lamfalussy process: Level 1 provisions + Level 2 implementing measures
- ✓ CESR's Advice forms the basis of Level 2 implementing measures

- Commission Regulation no. 583/2010 on KII was adopted on 1 July 2010

The policy and legislative process (2)

Policy steps

- April 2007: Commission' mandate to CESR for assistance on KII
- February 2008: CESR Preliminary Advice on KII (CESR/08-087)
- March-May 2009: CESR Consultation on KII (CESR/09-047)
- March 2008 – June 2009: European Commission's consumer testing
  - ✓ 2 phases: individual elements + mocked-up KII documents
  - ✓ Intermediaries testing
- **November 2009: publication of Directive 2009/65/EC (UCITS IV)**
- December 2009: CESR Final Advice on KII (09-949; 09-1026; 09-1028)
- July 2010: CESR Guidelines on the Synthetic Risk and Reward Indicator (CESR/10-673) and the presentation of Charges in the KII (CESR/10-674)

The policy and legislative process (3)

Policy steps

- **July 2010: adoption of EC Regulation no. 583/2010 on KII – according to Article 78 (7) of Directive 2009/65/EC**
- July-September 2010: CESR Consultation on new set of guidelines (below)
- December 2010: CESR adopts Guidelines on:
  - ✓ performance scenarios in the KII of structured UCITS (CESR/10-1318)
  - ✓ transition from the SP to the KII (CESR/10-1319)
  - ✓ language and layout for the KII (CESR/10-1320)
  - ✓ template for the KII document (CESR/10-1321)
- 1st of July 2011: **date of application of all UCITS IV package** (level 1 and 2) including the provisions on KII

3. Objectives and Principles of the KII

Objectives and Principles of the KII (1)

CESR's February 2008 Technical Advice

"*…the KID (KII) should fundamentally be a tool for helping retail consumers to reach informed investment decisions.....*

the KID should contain only the essential elements for making and carrying out those decisions, and should not be encumbered with information serving only legal or regulatory requirements.

Nor should it primarily be a marketing or investor education document.

Since its use is limited to providing pre-contractual information, it need not address investors' information requirements on an ongoing basis after they have invested.

A KID should be produced for all UCITS funds, and delivered to all investors in those funds."

Objectives and Principles of the KII (2)

<u>Article 78 of UCITS IV Directive</u>

"*1. Member States shall require that an investment company and, for <u>each of the common funds it manages</u>, a management company draw up a short document containing key information for investors…..*

2. Key investor information shall include appropriate information about the <u>essential characteristics</u> of the UCITS concerned, which is to be provided to investors so that they are reasonably able to understand <u>the nature and the risks</u> of the investment product that is being offered to them ….

5. Key investor information shall be written in a concise manner and in non-technical language. It shall be drawn up in a common format, <u>allowing for comparison</u>, and shall be presented in a way that is likely to be understood by retail investors."

Objectives and Principles of the KII (3)

Article 79 of UCITS IV Directive - Article 3 of KII Regulation

"1. Key investor information shall constitute pre-contractual information. It shall be fair, clear and not misleading." (**impact on liability**)

Article 80 of UCITS IV Directive

Investors shall be provided the KII "*in good time before their proposed subscription of units of UCITS*". (**mandatory delivery –** not only available)

Article 3 of KII Regulation

"1. This Regulation specifies in an exhaustive manner the form and content of the document containing key investor information ….. No other information or statements shall be included except where this Regulation states otherwise." (**maximum harmonization** – facilitates comparability)

4. Structure of the KII

Structure of the KII

<u>Article 78 (3) of UCITS IV Directive</u>

The KII shall provide information on the following essential elements:

a) *identification of the UCITS;*

b) *a short description of its investment objectives and investment policy;*

c) *past-performance presentation or, where relevant, performance scenarios;*

d) *costs and associated charges; and*

e) *risk/reward profile of the investment, including appropriate guidance and warnings in relation to the risks associated with investments in the relevant UCITS.*

KII Structure Investment policy (1)

Description of the investment policy (Art. 7 of KII Reg.) covers the essential "financial" and "operational" features of the fund. Among others, these include:

- the main categories of the financial instruments that eligible for investment;
- whether the UCITS allows for discretionary choices in regards to the investments, or whether this "*includes or implies*" a reference to a benchmark;
- where reference to a benchmark is implied, the "*degree of freedom*" available in relation to this benchmark shall be indicated;
- for "structured" UCITS, an explanation of the elements necessary to understand the pay-off, including, if necessary, the details on the algorithm that appears in the (full) prospectus;

KII Structure → Investment policy (2)

123 Fund, a sub-fund of ABC Fund SICAV (ISIN: 4321)
This fund is managed by ABC Fund Managers Ltd, part of the XYZ group of companies

Objectives and Investment Policy

Joint description of the objectives and policy of the UCITS in plain language (it is suggested not to copy-out the prospectus)

Essential features of the product which a typical investor should know:

- main categories of eligible financial instruments that are the object of investment
- a statement that the investor may redeem units on demand, and how frequently units are dealt in
- whether the UCITS has a particular target in relation to any industrial, geographic or other market sectors or specific classes of assets
- whether discretionary choices regarding particular investments are allowed, and whether the fund refers to a benchmark and if so which one
- a statement of whether any income arising from the fund is distributed or reinvested

Other information if relevant, such as:

- what type of debt securities the UCITS invests in
- information regarding any pre-determined pay off and the factors expected to determine performance
- if choice of assets is guided by growth, value or high dividends
- how use of hedging / arbitrage / leverage techniques may determine the fund's performance
- that portfolio transaction costs will have a material impact on performance
- minimum recommended holding term

KII Structure Risk and Reward (1)

Article 8 of the KII Regulation

"1. The 'Risk and reward profile' section of the key investor information document shall contain a synthetic indicator, supplemented by:

(a) a narrative explanation of the indicator and its main limitations;

(b) a narrative explanation of risks which are materially relevant to the UCITS and which are not adequately captured by the synthetic indicator.

2. The synthetic indicator referred to in paragraph 1 shall take the form of a series of categories on a numerical scale with the UCITS assigned to one of the categories…"

The Synthetic Risk and Reward Indicator (SRRI) is a major innovation of the KII. It is pillar for the comparability of funds.

KII Structure → Risk and Reward (2)

Risk and Reward Profile

Lower risk — Higher risk

Typically lower rewards — Typically higher rewards

1	**2**	3	4	5	6	7

Narrative explanation of the indicator and its main limitations:

- Historical data may not be a reliable indication for the future
- Risk category shown is not guaranteed and may shift over time
- The lowest category does not mean 'risk free'
- Why the fund is in its specific category
- Details of nature, timing and extent of any capital guarantee or protection

Narrative presentation of risks materially relevant to the fund which are not adequately captured by the indicator:

- Credit risk, where a significant level of investment is made in debt securities
- Liquidity risk, where a significant level of investment is made in financial instruments that are likely to have a low level of liquidity in some circumstances
- Counterparty risk, where a fund is backed by a guarantee from, or has material investment exposure through contracts with, a third party
- Operational risks including safekeeping of assets
- Impact of any techniques such as derivative contracts

KII Structure Risk and Reward (3)

1. CESR proposed the use of a SRRI in its October 2009 Advice to the EC.

2. CESR reached that conclusion after two consultations with stakeholders, (spring/summer 2009), and on grounds of the results of the testing from the EC.

3. The adoption of the SRRI required agreement on the methodology for the calculation of such indicator, in order to ensure that all UCITS are classified in the risk/reward scale according to the same criteria across the EU.

4. CESR developed a detailed methodology for the computation of the SRRI after having intensively consulted both regulators and industry representatives.

5. This methodology is set out in CESR's Guidelines (10-673) "*on the methodology for the calculation of the synthetic risk and reward indicator in the Key Investor Information Document*".

KII Structure Risk and Reward (4)

The SRRI methodology is meant to satisfy the following criteria:

✓provide indication of the <u>overall</u> risk and reward profile of the UCITS;

✓ensure an appropriate spread of UCITS across different risk classes;

✓applicable to <u>all</u> types of UCITS;

✓leave no room for manipulation;

✓enable easy and cost-effective implementation by UCITS providers;

✓be easily understood by auditors, advisers and distributors;

✓enable easy and effective supervision by regulators; and

✓achieve an adequate degree of stability in the risk classification process with respect to <u>normal trends and fluctuations</u> of financial markets.

KII Structure ⇨ Risk and Reward (5)

The SRRI methodology is fundamentally built on the volatility of the fund during the last 5 years.

Stability vs. accuracy issue tackled by risk migration rules (4 months breach).

$$p = \textit{time unit}$$

$$T = \textit{lenght of the temporal sample}$$

$$n = \textit{number of observations} = T / p$$

$$t_i = \textit{date of the } i^{th} \textit{ observation in the sample}$$

$$i \in [1, 2, 3 \ldots\ldots n-1, n]$$

$$r_i = \frac{NAV_{t_i} - NAV_{t_{i-1}}}{NAV_{t_{i-1}}} \simeq \ln\left(\frac{NAV_{t_i}}{NAV_{t_{i-1}}}\right) \textit{ if } p \textit{ is small}$$

$$\mu = \frac{\sum_{i=1}^{n} r_i}{n}$$

$$vol = std = \sigma = \sqrt[2]{\frac{\sum_{i=1}^{n} (r_i - \mu)^2}{(n-1)}} \times \sqrt[2]{\frac{1 \textit{ year}}{p}}$$

Risk Class	Volatility Intervals	
	equal or above	less than
1	0%	0.5%
2	0.5%	2%
3	2%	5%
4	5%	10%
5	10%	15%
6	15%	25%
7	25%	

KII Structure → Risk and Reward (6)

To calculate the volatility of the fund 5 years of its weekly returns are generally needed.

However, the methodology also addresses those cases when data on returns are missing, or not meaningful; notably for:

- Funds with insufficient performance history (UCITS newly established or that have changed investment policy over time)

- Absolute return funds
- Total return funds
- Life cycle funds

Funds with predetermined risk or reward targets

→ **Strategy funds:** do not follow a market but a strategy. Have an actively managed dynamic asset mix

- Structured funds (funds that offer returns linked to the performance of financial assets, indices or reference portfolios)

KII Structure Past Performance (1)

Article 15 of the KII Regulation

1. The information about the past performance of the UCITS shall be presented in a bar chart covering the performance of the UCITS for the last 10 years. (beyond MiFID requirements)

2. UCITS with performance of less than 5 complete calendar years shall use a presentation covering the last 5 years only.

3. For any years for which data is not available, the year shall be shown as blank with no annotation other than the date.

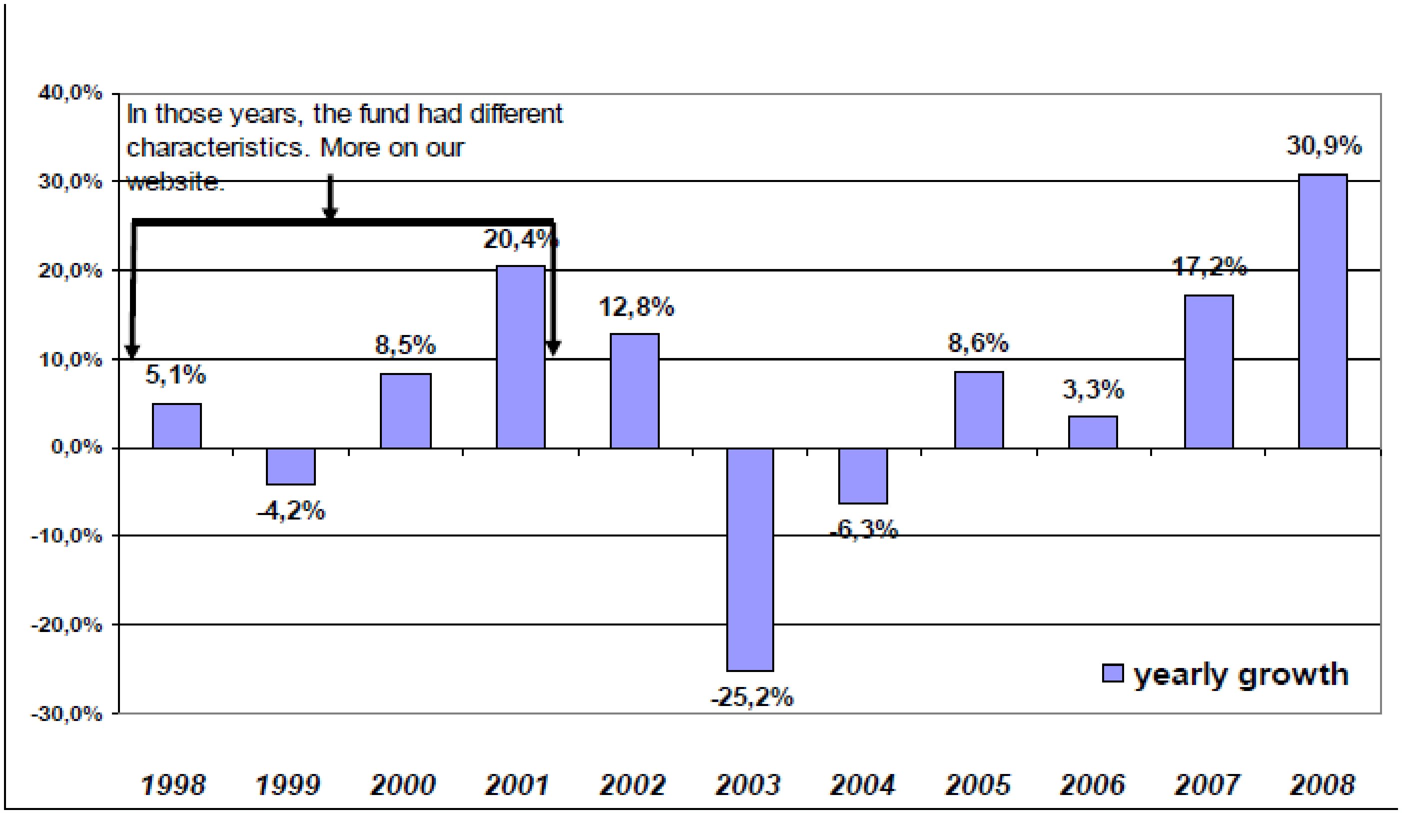
-The chart to be accompanied by important warnings on past performance (no forecast of future performance, entry/exit charges not considered, ect…)

- The performance is calculated including income distributed by the fund.

- Clear indication of the currency in which the NAV is calculated

KII Structure Past Performance (2)

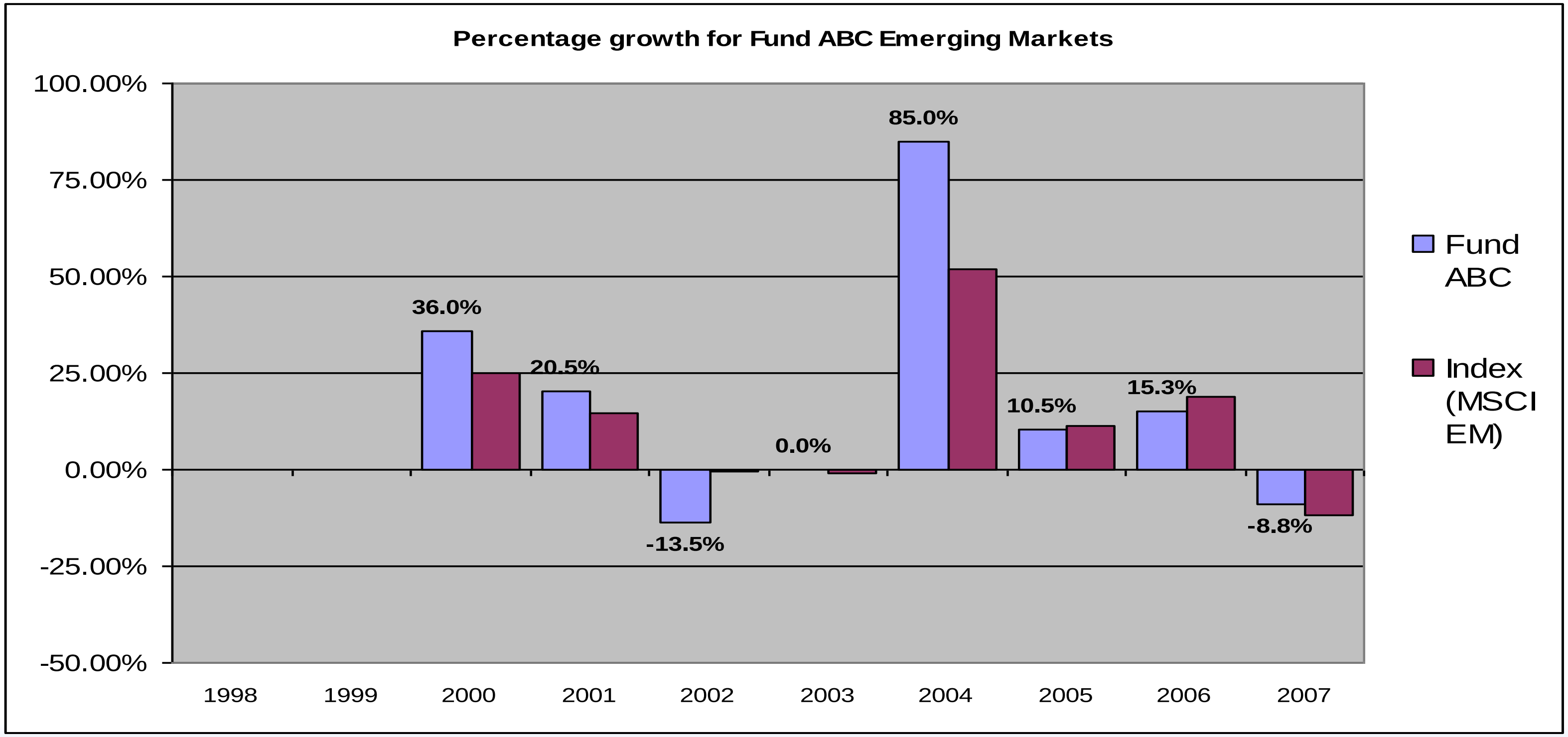
If a UCITS changes its investment policy, the past performance prior to that change shall continue to be shown (against moral hazard), but with a clear warning that those circumstances no longer apply (Art.17 of KII Regulation).



KII Structure Past Performance (3)

<u>Article 18 of the KII Regulation</u>

Where the 'Objectives and investment policy' section of the key investor information document makes reference to a benchmark,…the performance of that benchmark shall be included in the chart alongside ..[that of]..*the UCITS.*



KII Structure Charges (1)

The mandate from the EC asked CESR to consider:

- developing summary figures to show fund charges and fees
- the presentation of the effect of charges via examples in cash terms
- options for a single cost figure summarising all charges

KII Structure Charges (2)

Consumer preferences revealed…

Improved Narrative (Option A)

v

Improved narrative + summary figure (Option B)

Illustration of Charges Text Version

v

Illustration of Charges Table Version

KII Structure Charges (3)

The costs paid by the investor (on the amount invested) and the fees charged to the UCITS should be presented in a table (Art. 10 of KII Reg.). In particular:

a) entry and exit charges shall each be the maximum percentage which might be deducted from the investor's capital commitment to the UCITS;

b) a single figure shall be shown for charges taken from the UCITS over a year, to be known as the 'ongoing charges,' representing all annual charges and other payments taken from the assets of the UCITS over the defined period, and based on the figures for the preceding year; (management fees)

c) the table shall list and explain any charges taken from the UCITS under certain specific conditions, the basis on which the charge is calculated, and when the charge applies. (performance fees)

KII Structure Charges (4)

One-off charges taken before (or after) you invest	
Entry charge	1.50%
This is the maximum that might be taken out of your money before it is invested (before the proceeds of your investment are paid out)	
Charges taken from the fund over a year	
Ongoing charges	0.75%
Charges taken from the fund under certain specific conditions	
Performance fees 15% a year of any returns the fund achieves above our benchmark for these fees, Alfa Capital Euro Aggregate Bond Index	

- if a range is set out in the FP (or fund rules), the KII shall indicate the maximum entry/exit charge

- ongoing charges are based on the last year's expenses (non audited accounts can be used);

however, estimates are used:

a) in case of all inclusive fees

b) when maximum fees are capped

c) after material changes to fees

KII Structure Charges (5)

CESR Guidelines clarifies that ongoing charges **shall reflect** all costs borne by the UCITS, whether they represent expenses incurred in the operation, or the remuneration of any party connected with it or providing services to it. Typically, these costs include payments to:

- the management company of the UCITS;
- the depositary/ custodian(s);
- the investment adviser(s);
- all payments to any person providing outsourced services (providers of valuation and fund accounting services, transfer agents, broker /dealers..);
- registration fees, regulatory fees and similar charges;
- audit fees;
- payments to legal and professional advisers;
- any costs of distribution/martketing.

KII Structure Charges (6)

On the contrary, CESR Guidelines clarifies that ongoing charges shall **not** include the transaction costs relating to the acquisition or disposal of assets, apart from those (entry/exit fees) linked to investments in other funds.

The rationale for this exemption is that transaction costs cannot be always easily identified (embedded in asset prices).

..however, according to Article 12(2) of the KII Regulation:

"*Where the impact of portfolio transaction costs on returns is likely to be material due to the strategy adopted by the UCITS, this shall be stated within the 'Objectives and investment policy' section*.. [of the KII]"

- a UCITS that invests a substantial proportion (+/- more than 5%) of its assets in other funds shall use the TERs (total expense ratio) of those funds in the calculation of its ongoing charges. Rebates of fess can be deducted.

KII Structure ⇨ Practical Information

- The Practical Information provides the following information, as relevant to investors in every Member State where the UCITS is marketed:

(a) the name of the depositary;

(b) where/how to obtain: the Full Prospectus (FP) of the UCITS, its latest annual and half-yearly report, indicating the language of those documents;

(c) where/how to obtain other practical information, including where to find the latest prices of units;

(d) a statement that the tax legislation of the UCITS' home Member State may have an impact on the personal tax position of the investor.

- Where applicable, this section will include information on the share classes of the UCITS available to (retail) investors.

5. Format and presentation of KII

Format and presentation of KII (1)

According to Article 5 of the KII Regulation, the KII shall be:

(a) *presented and laid out in a way that is easy to read, using characters of readable size;*

(b) *clearly expressed and written in language that communicates in a way that facilitates the investor's understanding of the information being communicated, in particular where:*

(i) *the language used is clear, succinct and comprehensible;*

(ii) *the use of jargon is avoided;*

(iii) *technical terms are avoided when everyday words can be used*

Article 6 of the KII Regulation

The key investor information document shall not exceed two pages of A4-sized paper when printed.

Format and presentation of KII (2)

CESR's Guidelines (10-1320) on language and layout of KII explains:

- use of plain language is not about dumbing-down or avoiding complex concepts. Instead it means:

a) writing so that your audience is not alienated by unfamiliar and pompous vocabulary and convoluted construction;

b) giving complex information in a clear way.

- investors may easily become frustrated if have to re-read the information

- use of plain language may require the 'unlearning' of habits inherited from the traditional formal or legalistic ways of writing fund documents. Nothing is gained by the presumed certainty of legalistic, technical or complex language, if the reader does not understand it or, worse, is misled by it.

Format and presentation of KII (3)

- **Avoid jargon**: use of specialist language should be minimum.

Jargon can be tackled by:

- explaining the feature without naming it. For example, saying that a performance fee includes a feature known as a high watermark does not necessarily help to explain what it is;
- explaining jargon in brackets after its first use;
- explaining jargon in a footnote to the section or the page;
- cross-referring to a glossary in a supporting document.

- **Cross-references** are permitted to (a part of) the website of the UCITS or the management company containing the FP and the periodic reports.

Cross-references shall in any case direct the investor to the specific section of the relevant document and shall be kept to a minimum.

Format and presentation of KII (4)

- **Explain risks** that are not adequately reflected by the SRRI according to their materiality (impact and probability).

It is necessary to go beyond a bald statement of the risks by briefly explaining their implications to the investor. For example: how much of the fund is being exposed to a particular risk, how likely it is that the risk will materialise, and how severe the impact would be if it did.

The typical risks that may not be fully captured by the synthetic indicator are: counterparty, default, liquidity, operational (various emerging market) risks.

- Explain if the risk is modified by a legally enforceable guarantee.

- Explain the implications of cashing in the investment outside of any associated set period (crucial for guaranteed, protected or structured funds).

Format and presentation of KII (5)

- **Use a legible type size**, balancing line width and line spacing:

- wide lines of small type are a problem for the eye to follow, keep characters in a line of 10-point, similarly to newspaper columns.

- typefaces vary, but when using the full width of A4 paper, aim for at least 11 pt fonts and 10 pt for sans serif fonts;

- keep the space between lines in balance with the type size.

- **Colour adds appeal**, but the KII may be photocopied or downloaded in black and white. If colours are used, enough contrast must be ensured between the text and its background – the effect is better if the text is dark and the background pale. It may therefore be better to use shading.

6. Specific cases

Specific cases (1)

<u>Article 78 (7) of the UCITS Directive and Chapter IV of the KII Regulation</u>

Particular Structures refer to:

1. Investment compartments
2. Funds of funds
3. Feeder funds
4. UCITS with different classes of shares/units
5. Structured UCITS

Specific cases (2)

➢ **Investment compartments**

- if a UCITS consists of different investment compartments a separate KII shall be produced for each compartment

- if investors pay a specific fee to shift from one compartment to another, that charge shall be indicated separately in the 'Charges' section of the KII

➢ **Funds of funds**

-if a UCITS invests a substantial proportion of its assets in other funds, the description of the objectives and investment policy of that UCITS in the KII shall include an explanation of how the target funds are to be selected

- the description of the risk factors in the KII shall cover the risks posed by each underlying fund, if these are material to the UCITS as a whole

Specific cases (3)

<u>Article 58 of the UCITS Directive</u>

*1. <u>A **feeder UCITS**</u> is a UCITS… which has been approved to invest, by way of derogation from Article 1(2)(a), Articles 50, 52 and 55, and Article 6(2)(c), at least 85 % of its assets in units of another UCITS ….*

2. A feeder UCITS may hold up to 15 % of its assets in one or more of the following:

(a) ancillary liquid assets in accordance with the second subparagraph of Article 50(2);

(b) financial derivative instruments, which may be used only for hedging purposes, in accordance with Article 50(1)(g) and Article 51(2) and (3);

….

Specific cases (4)

- **Feeder UCITS**

- the KII of the feeder should combine the costs of both the feeder and the master UCITS in the ongoing charges figure

- a feeder can show the past performance of its master as a benchmark;

- a feeder may "simulate" its performance by using that of its master when:

- its investment strategy and objectives do not allow it to hold assets other than units of the master and ancillary liquid assets; or
- the feeder's characteristics do not differ materially from those of the master.

Specific cases (5)

- **UCITS whit different classes of shares/units**

- if a UCITS has more than one class of units or shares, a different KII shall be prepared for each class of units or shares

- the UCITS may select a specific class to represent also other classes in a single KII, provided that this choice is fair, clear and not misleading. In these cases the 'Risk and reward profile' section of the KII shall illustrate the material risks applicable to any of the other classes

- a new share class of an existing UCITS may simulate its performance by using the performance of another class, provided the two classes do not differ materially in the extent of their participation in the assets of the UCITS

Specific cases ⇨ Structured UCITS (1)

Article 36 of the KII Regulation

*1. The key investor information document for **structured UCITS** shall not contain the 'Past performance' section.*

as these generally close subscriptions after initial offering…

*..**structured UCITS** shall be understood as UCITS which provide investors, at certain predetermined dates, with algorithm-based (*formula*) payoffs that are linked to the performance, or to the realisation of price changes or other conditions, of financial assets, indices or reference portfolios funds….*

[The KII of structured funds] *shall be accompanied by an illustration, showing at least three scenarios of the UCITS' potential performance. ... to show the circumstances in which the formula may generate a low, a medium or a high return, including, where applicable, a negative return ...*

Specific cases ⇨ Structured UCITS (2)

In its preliminary work, CESR analysed 3 options for structured UCITS:

Backtesting:

➢ Showing how the fund would have performed under historic market conditions

Many drawbacks have been identified in this methodology.

Prospective scenarios:

➢ Presentation of the possible performance of the fund under favourable, adverse, or "neutral" market conditions.

The scenarios could be presented either under the form of a graph or a table ✓

Probability tables:

➢ A table showing the probabilities that the expected performance of the UCITS over-performs, equalise or under-performs that of a risk free asset.

Consensus needed on the requirements applicable to the stochastic models used.

Specific cases ⇨ Structured UCITS (3)

1. Performance scenarios for structured funds shall be based on reasonable and conservative assumptions on future market conditions

2. According to CESR's Guidelines (10-1318), the scenarios shall present:

- the functioning of the formula under unfavourable, favourable and neutral market conditions (the unfavourable case shall be explained first);
- the specific features of the formula, for instance a capped performance, or a level of leverage;
- the situations where some mechanisms of the formula have a favourable or unfavourable impact on final performance.

3. The Guidelines have also clarified that, depending on the formula (e.g. knock-out feature or guarantee with conditional floor etc), more than three scenarios may be required to adequately describe the possible outcomes.

Specific cases ⇨ Structured UCITS (4)

1. If there is a conditional protection/guarantee, an additional (4^{th}) example should illustrate how extreme conditions can cause a capital loss.

2. The scenarios shall be called "Illustrative examples", it shall be clear that these are not forecasts and that they are not equally probable.

3. Performance scenarios shall be presented in either tables or graphs.

4. The graphs shall avoid:

- double scales (left and right) whenever possible;
- artificially magnifying the positive aspects of the fund payout;
- non-linear scales;
- different scales depending on the scenario.

Specific cases ⇨ Structured UCITS (5)

Example with tables

The final payout is the average of all the performances of each share in the basket. The performance is calculated as the underlying value of each share in the basket after 2 years with any growth capped at 9.5%. There is a legally enforceable guarantee of the return of the amount invested.

Unfavourable conditions (low return):

Share	Underlying performance	UCITS performance
1	-4%	-4.0%
2	-2%	-2.0%
3	-12%	-12.0%
4	-23%	-23.0%
5	0%	0.0%

Average performance of the basket of shares	-8.2%
UCITS performance	0%
Equivalent annual growth rate	0%

At the end date, the average performance of the basket is -8.2%, so the guarantee will apply.

If units are sold before maturity: the price will be based on the market value of the financial derivative instruments used and not the value of the underlying shares.

Specific cases ⇨ Structured UCITS (6)

Favourable conditions (high return):

Share	Underlying performance	UCITS performance
1	10%	9.5%
2	11%	9.5%
3	12%	9.5%
4	10%	9.5%
5	13%	9.5%

Basket of shares performance	11.2%
UCITS performance	9.5%
Equivalent annual growth rate	4.65%

Therefore, an investment kept until the end date, would pay out only 9.5% of the amount invested.

Medium conditions (medium return):

Share	Performance	Performance Retained
1	2%	2.0%
2	0	0.0%
3	8%	8.0%
4	-5%	-5.0%
5	11%	9.5%

Basket of shares performance	3.2%
UCITS performance	2.9%
Equivalent annual growth rate	1.44%

At the end date, the average performance of the basket is 3.2%, and the UCITS performance will be only 2.9% because of the cap on one of the shares in the basket. This corresponds to an annual growth rate of 1.44%.

Specific cases ⇨ Structured UCITS (7)

If at an annual measurement date, Eurostoxx is at least at its level on the start date, the payout is the original investment increased by 8% for each of the years since the start date. If this happens at the end of the second year onwards, the equivalent annual growth rate will be less than 8%.

If at each annual measurement date, the performance of the Eurostoxx index remains below its level at the start date, the payout after 8 years depends upon the CAC 40 index.

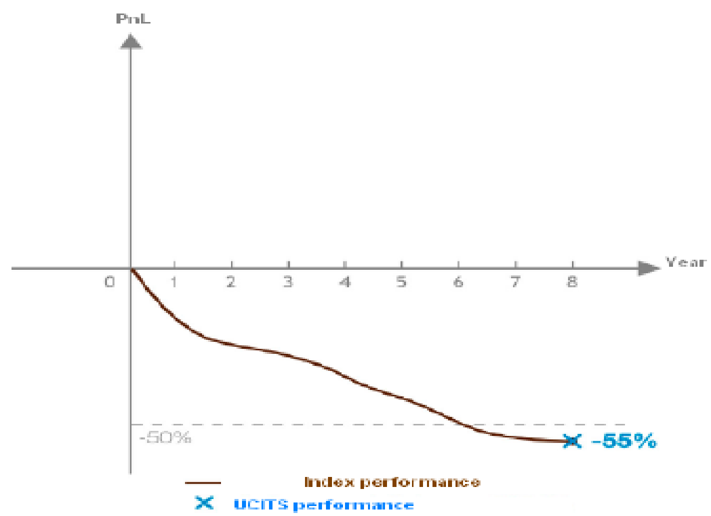
- If the CAC 40 index has dropped by 50% or less since the start date, the original investment is paid back.
- If the CAC 40 index has dropped by more than 50% since the start date, the payout is the amount originally invested reduced by the percentage decrease in the Eurostoxx index.

Investors' capital is therefore at risk.

Very unfavourable conditions (low return):

The Eurostoxx index remains below the level at the start for 8 years so the plan does not pay out early.

After 8 years, the level of the CAC 40 index is less than 50% of its level at the start date, which means that the payout is less than the amount originally invested.



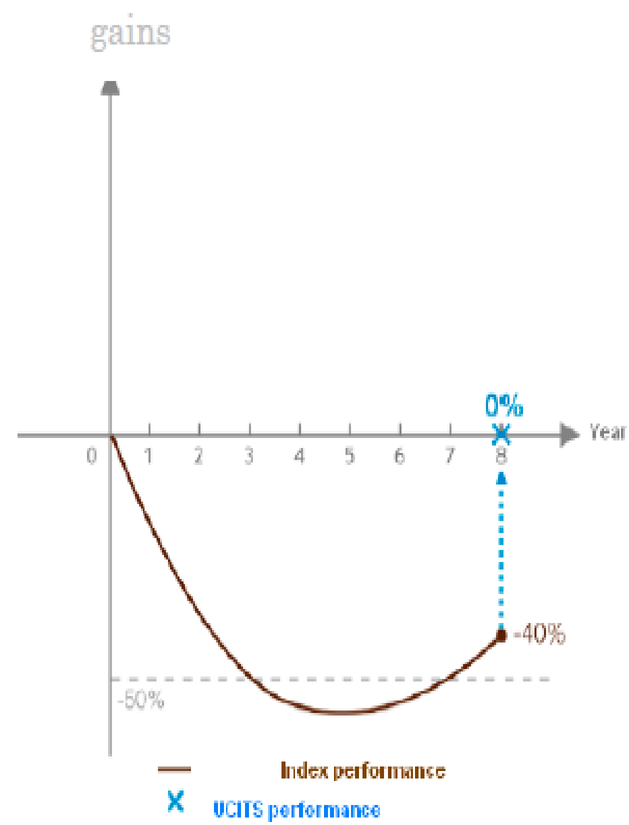
Example with graphs

Specific cases ⇨ Structured UCITS (8)

Unfavourable conditions (low return):

The Eurostoxx index remains below the level at the start for 8 years so the plan does not pay out early.

But after 8 years the CAC 40 index has not reduced by more than 50% of its level at the start, so the payout is the amount originally invested.



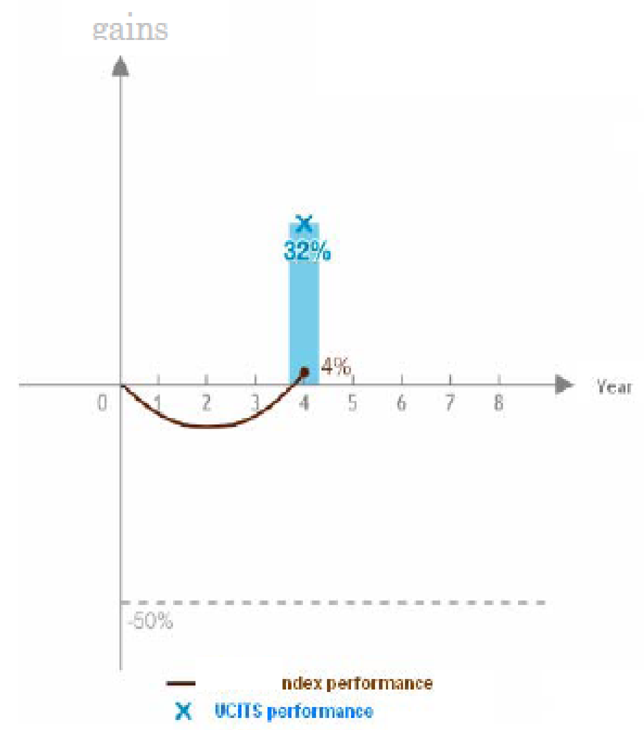
Specific cases ⇨ Structured UCITS (9)

Favourable conditions (high return):

The Eurostoxx index goes above its level at the start date for the first time at the 4th measurement date.

The plan will then pay out the original investment plus 32% (4 x 8%) , so a €1,000 investment would grow to €1320

The equivalent annual growth rate would then be 7.18%.



If units are sold before the end date: the price will not be calculated using the formula but will be based on the net asset value of the UCITS which will include the market value of the financial derivative instruments used.

Specific cases ⇨ Structured UCITS (10)

1.Given the inclusion of the performance scenarios the KII of Structured UCITS can reach <u>3 A4-sized pages</u> (Article 37 of KII Regualtion)

2. The performance scenarios shall be updated:

- if market conditions have changed significantly since the launch;
- at least on a yearly basis;
- to reflect the time-dependency of a payoff, if any and relevant (e.g. where an anniversary date has passed)

3. A narrative shall explain investors that they can always sell/redeem their units before the end-date of the structured UCITS, but it shall also include a warning regarding possible losses in those circumstances, as the pay-off will not be calculated using the formula but will simply reflect the market value of the underlying assets at the time of the sale/redemption.

KII Template: page1

Key Investor Information Document

This document provides you with key investor information about this fund. It is not marketing material. The information is required by law to help you understand the nature and the risks of investing in this fund. You are advised to read it so you can make an informed decision about whether to invest.

123 Fund, a sub-fund of ABC Fund SICAV (ISIN: 4321)

This fund is managed by ABC Fund Managers Ltd, part of the XYZ group of companies

Objectives and investment policy

- Joint description of the objectives and policy of the UCITS in plain language (It is suggested not to copy out the prospectus)
- Essential features of the product which a typical investor should know:
  - main categories of eligible financial instruments that are the object of investment
  - a statement that the investor may redeem units on demand, and how frequently units are dealt in
  - whether the UCITS has a particular target in relation to any industrial, geographic or other market sectors or specific classes of assets
  - whether discretionary choices regarding particular investments are allowed, and whether the fund refers to a benchmark and if so which one
  - a statement of whether any income arising from the fund is distributed or reinvested
- Other information if relevant, such as:
  - what type of bonds the UCITS invests in
  - information regarding any pre-determined pay off and the expected performance drivers
  - if choice of assets is guided by growth, value or high dividends
  - minimum recommended holding term
  - how use of hedging / arbitrage / leverage techniques may determine the fund's performance
  - that portfolio transaction costs will have a material impact on performance

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Risk and reward profile

⇦Typically lower rewards Typically higher rewards ⇨
⇦ Lower risk Higher risk ⇨

1	**2**	3	4	5	6	7

Narrative explanation of main limitations of the indicator:

- Historical data may not be a reliable indication for the future
- Risk category shown is not guaranteed and may shift over time
- The lowest category does not mean 'risk free'
- Why the fund is in its specific category
- Details of nature, timing and extent of any capital guarantee or protection

Narrative presentation of risks materially relevant to the fund which are not adequately captured by the indicator:

- Credit risk, where a significant level of investment is made in debt securities
- Liquidity risk, where a significant level of investment is made in financial instruments that are likely to have a low level of liquidity in some circumstances
- Counterparty risk, where a fund is backed by a guarantee from, or has material investment exposure through contracts with, a third party
- Operational risks including safekeeping of assets
- Impact of any techniques such as derivative contracts

KII Template: page2

Charges

The charges you pay are used to pay the costs of running the fund, including the costs of marketing and distributing it. These charges reduce the potential growth of your investment.

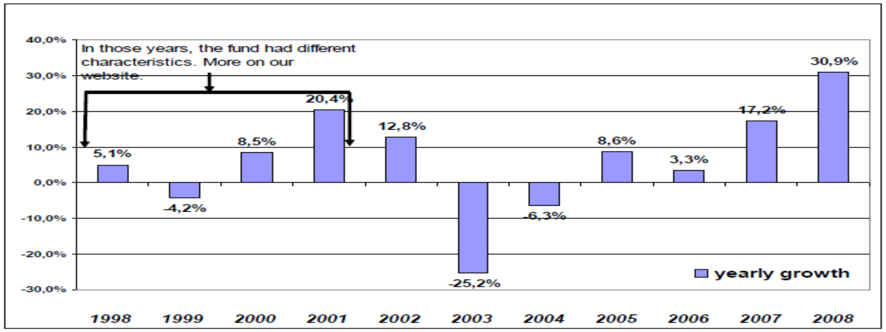
One-off charges taken before or after you invest	
Entry charge	[ ]%
Exit charge	[ ]%
This is the maximum that might be taken out of your money [before it is invested] [before the proceeds of your investment are paid out].	
Charges taken from the fund over each year	
Ongoing charges	[ ]%
Charges taken from the fund under specific conditions	
Performance fee	[ ]% a year of any returns the fund achieves above its benchmark, the [insert name of benchmark].

For more information about charges, please see [pages x to x / section x] of the fund's prospectus which is available at www.ucitsfund/prospectus

The ongoing charges figure excludes

- Performance fees
- Portfolio transaction costs, except in the case of an entry/exit charge paid by the UCITS when buying or selling units in another collective investment undertaking

Past performance



- The chart will be supplemented with prominent statements which:
  - warn about its limited value as a guide to future performance
  - indicate briefly which charges have been included or excluded
  - state the year when the fund started
  - indicate the currency in which past performance has been calculated.

Practical information

- Name of the depositary
- Where and how to obtain further information about the UCITS (prospectus, reports & accounts)
- Where and how to obtain other practical information (e.g. where to find latest unit prices)
- A statement that tax legislation of the fund's Home State may have an impact on the personal tax position of the investor
- A statement that "[Name of management company] may be held liable solely on the basis of any statement contained in this document that is misleading, inaccurate or inconsistent with the relevant parts of the prospectus for the fund"
- Specific information relating to umbrella funds (e.g. any switching rights between sub-funds)
- Information about other share classes, if applicable (KID may be based on a representative class)

This fund is authorised in [name of Member State] and regulated by [identity of competent authority]. [Name of management company] is authorised in [name of Member state] on [date] and regulated by [identity of competent authority]. This key investor information is accurate as at [date of publication].

..a final comment

<u>Let's recall the basic overarching principles of the KII</u>

Article 78 of UCITS IV Directive

"*1. Member States shall require that an investment company and, for <u>each of the common funds it manages</u>, a management company draw up a short document containing key information for investors.....*

*2. Key investor information shall include **appropriate information** about the <u>**essential characteristics**</u> of the UCITS concerned, which is to be provided to investors so that they **are reasonably able to understand** the **nature and the risks** of the investment product that is being offered to them ....*

*5. Key investor information shall be written in a **concise manner and in non-technical language**. It shall be drawn up in a common format, allowing for comparison, and shall be presented in a way that is likely to be **understood by retail investors**."*

..a final comment

THE KII MUST BE

SIMPLE, **CLEAR**, **CONCISE**

..but also

MEANINGFUL and **PRECISE**

...to be essential and at the same time concise information must be processed and elaborated with care...

can take longer preparing a KII than a much lengthier SP !

"*I didn't have time to write a short letter, so I wrote a long one instead*." (Blaise Pascal)

Thank you very much !

Francesco Maria de Rossi
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francesco.derossi@esma.europa.eu

Key Information Document for retail investors

Q&A session