



MiFID II – Distributor Q&A

1. Introduction

This briefing note provides further background and information of the main areas we anticipate will arise in discussions with Distributors regarding the impact of MiFID II.

2. Definitions under MiFID II – Who is a Distributor?

The MiFID II definition of a Distributor is very broad. It is set out in Commission Delegated Directive C(2016) 2013 Recital 15 as follows:

“...Investment firms that offer or sell financial instruments and services to clients should be considered distributors.”

Vanguard is not able to provide advice or guidance around the definition of a “distributor” under MiFID II. It is up to the firm in question to determine if they are distributor of Vanguard products under MiFID II.

3. Obligations of Manufacturers & Distributors

MiFID II requires a clear and formal relationship between a Manufacturer and its Distributors.

In order to meet the obligations of MiFID II Vanguard requires agreements to be in place with Distributors. There is often a chain of Distributors involved in these cases. We only require an agreement with the first Distributor in the chain (the Distributor who buys and sells our Funds with our Transfer Agent) this will often be a Platform. The primary distributor will then have agreements in place with sub-distributors. The agreement can follow our template or one provided by the Distributor.

Where we have a distribution agreement in place, we will be updating the terms to include MiFID II language by way of an annex. We consider that this is necessary because whilst our existing contract’s applicable law provisions may mean that compliance with MiFID II is mandated, there is no provision in existing documentation for the practicalities of information exchange obligations brought in by MiFID II (i.e. periodicity, recipients, format) which our annex amongst other things looks to address. Our annex merely shows that there is no ambiguity on interpretation of MiFID II.

4. Target Market Information

It is a requirement of MiFID II that a Manufacturer documents a Target Market for each product and communicates this to Distributors. The Distributor is then responsible for documenting its own target market and ensuring the target markets of the Product are therefore aligned.

Vanguard has prepared Target Market descriptions for all funds in accordance with the The European Securities and Markets Authority (ESMA) Consultation and the European MiFID Template (EMT) template agreed by industry working groups.

We expect that many Distributors will want to receive this information from the usual data vendors and we are making this available in this way. Vanguard will also publish a short, written document setting out its product approval process to enable Distributors to meet their requirements in this regard.

5. Information that Vanguard requires from Primary Distributors

As a Manufacturer Vanguard has obligations under MiFID II to ensure that its Products are reaching the Target Market and Distributors are required to provide information to enable this.

We will adopt a standard industry approach for sales measurements (MI) in line with Tax Incentivised Savings Association (TISA) UK and ESMA industry recommendations and therefore we expect to be asking Distributors for the same information that other providers will request.

6. Negative Target Market Reporting

We do not expect our funds to be sold into a negative target (i.e. clients which (a) require full capital protection and / or seeking on-demand full repayment of the amounts invested (b) are fully risk averse/have no risk tolerance) but if this happens we will require distributors to notify us by exception.

7. Know Your Distributor (KYD)

Under MiFID II, a manufacturer needs to have an understanding of the type of activity a Distributor undertakes including the type of end clients. This understanding is necessary to help the Manufacturer ensure that its Products are being distributed in a way which is consistent with the Target Market.

Vanguard is addressing this in a number of ways. We expect our sales people to get to know Distributors better and so ask questions concerning the nature of the business and the end clients. This level of understanding should also help Vanguard to understand which of our funds are more compatible with the needs of the end investors. This will be integrated into the Miller Heiman sales process.

Vanguard will also be asking Primary Distributors to provide certain information and complete a Due Diligence Questionnaire "DDQ", Wolfsberg Questionnaire and provide AML documentation for review. The DDQ template is consistent with other fund providers and we will accept the templates of our distributors where they are of a suitable standard in order to minimise the amount of effort required to respond.

8. Complex Products and the Appropriateness Test.

MiFID II requires Distributors to undertake an appropriateness test before selling 'complex' products to Retail investors without advice.

It is for Distributors to determine whether a MiFID II 'Appropriateness test' is required when distributing Products to investors, including when a product is 'complex'. As a manufacturer we can state that we do not believe that any Vanguard UK or Irish Fund fall within the MiFID definition of 'Complex'.

All our funds are UCITs and are therefore "non- complex" and suitable for "mass retail".

9. Share Class characteristics/Suitability – "MiFID II compliant share classes"

We do not pay retrocession to promote distribution. Therefore all our share classes are clean and we do not anticipate launching any new share classes for MiFID.

Please also note that whilst we may name the share classes "institutional" the target market is in fact the same as the "investor" classes (i.e retail investors could potentially invest in the Institutional share classes provided they meet the minimum holding amounts). For the purposes of MIFID we will be assessing the target market at the sub-fund level and not at share class level.

10. Costs and Charges Disclosure

MiFID II requires costs and charges information to be provided to investors both ex-ante and ex-post. Distributors will need to add their own costs and charges when presenting this information to the end investors.

Information is provided using the EMT which is available via data vendors e.g. Financial Express, Funds Library, Morningstar and on our website.

Please see Costs and Charges Q&A for further information

11. PRIIPs

We are utilising the UCITS exemption which has been extended to the end of 2021 for our existing UCITS funds, which means that we will not be providing a PRIIPs KID at this stage. However as our UCITS funds are available through PRIIPS wrappers provided by various Life companies, we will be providing PRIIPs information to insurers through the industry standard European PRIIPs Templates (EPT).

After the end of December 2021 we expect to produce our own PRIIP KIDs as well as continuing to send the EPT. We will also continue to produce the UCITS KIID until there is confirmation from the EU Commission/Parliament's review that it is to be replaced by the PRIIP KID.

Please see PRIIPs Q&A for further information

12. Non-EU Distributors

As VAM is involved in the product design and development process, all our UCITS funds regardless of whether UK or Irish will be subject to the product governance requirements as VAM will be characterized as a "manufacturer";

Therefore, it does not matter that VGIL enters into the distribution agreements with US intermediaries to distribute products in non-EU countries because VAM is involved in the

design of these products it will be classified as a manufacturer.

As a result, distribution in the following regions, by virtue of them selling Irish UCITS, will be impacted to some extent by Europe's MiFID II regulation:

- Switzerland (they will be adopting equivalent rules)
- Latin America
- Asia

Although these jurisdictions are not bound by MiFID II we still have an obligation to make available target market information and request sales MI (on a proportionate basis).

For more information in relation to the above Q&A please send an email to european_client_services@vanguard.co.uk

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VAM: 1064086