

Technical Advice on delegated acts to supplement Regulation (EU) 2019/1238 (PEPP Regulation) with regard to criteria and factors to be applied by EIOPA in relation to EIOPA's product intervention powers

Extract from the Call for Advice

3.1 Criteria and factors to determine when there is a significant PEPP saver protection concern, for the purpose of EIOPA's intervention powers (as laid down in the empowerment of Article 65(2) of the PEPP Regulation)

The PEPP Regulation confers on EIOPA the power to monitor the market for PEPPs which are marketed, distributed or sold in the Union and, subject to certain conditions, temporarily prohibit or restrict in the Union the marketing, distribution or sale of certain PEPPs or PEPPs with certain specified features.

While these powers need to be applied in a proportionate way, and are expected to be of an extraordinary nature or constitute a measure of last resort², there is also a need to ensure that such powers are dynamic enough to address significant risks that may arise in the markets.

Under article 65(9) of the PEPP Regulation, the Commission shall adopt, in the context of product intervention powers for EIOPA, delegated acts to supplement the PEPP Regulation with "*criteria and factors to be applied by EIOPA in determining when there is a significant PEPP saver protection concern, including with respect to the long-term retirement nature of the product, or a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union referred to in point (a) of paragraph 3*" of the PEPP Regulation.

The PEPP Regulation already provides a framework for EIOPA's product intervention powers and lays down that the criteria and factors to be applied by EIOPA, in determining when there is a significant PEPP saver protection concern (including with respect to the long-term retirement nature of the product), or a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union, shall include:

- (a) the degree of complexity of the PEPP and the relation to the type of PEPP saver to whom it is marketed and sold;
- (b) the degree of innovation of a PEPP;

- (c) the leverage of a PEPP;
- (d) in relation to the orderly functioning and integrity of financial markets, the size or the total amount of accumulated capital of the PEPP.

Those criteria and factors shall take into account the result of any relevant work conducted by EIOPA, in particular relating to the PRIIPs Regulation, and by ESMA and EBA under MIFIR and the ESAs' experiences related to their product intervention powers. EIOPA may differentiate between situations where EIOPA takes action because a competent authority has failed to act and situations where EIOPA takes action because the actions that have been taken by the competent authorit(ies) do not adequately address the significant PEPP saver protection concern (including with respect to the long-term retirement nature of the product) or the threat to the orderly functioning and integrity of financial markets.

The factors may refer to the degree of complexity or innovation of a PEPP and its particular features, the type of PEPP savers to which the PEPP is marketed or sold and their financial sophistication. The factors and criteria can be linked to product features pertaining to, for example, the proposed investments, the risk-mitigation techniques, the cost structures, the corresponding governance structures, and the PEPP provider's business model. In relation to the orderly functioning and integrity of financial markets, the factors may also refer to the size or the total amount of accumulated capital of the PEPP, the potential scale of detriment in the market and to the individual's savings, possible contagion effect and where relevant, the detrimental effect on the price formation mechanism in the underlying market.

EIOPA may also elaborate on the interlinkage between individual criteria and the assessment of their collective effect leading to a significant PEPP saver protection concern or a threat to the orderly functioning and integrity of financial markets.

Those criteria and factors should ensure a sufficient degree of legal clarity, in order to allow a harmonised application of EIOPA's intervention powers. They should also ensure that EIOPA can intervene and react towards exceptional situations or new and evolving market products or practices. When preparing its technical advice, EIOPA should also duly take into consideration relevant cases-law³.

² That means a systematic prior approval of PEPPs' terms and conditions is not expected.

³ Judgment of the Court (Grand Chamber) of 22 January 2014, United Kingdom of Great Britain and Northern Ireland v European Parliament and Council of the European Union, Case C-270/12.

Previous advice

Not applicable.

Relevant legal provisions

The legal provision in place to take into account for this Advice is Article 65(9) of the PEPP Regulation.

Other regulatory background

Not applicable.

Criteria and factors to be applied

Background

For endorsing the PEPP quality label, the marketed and distributed PEPPs need to be monitored. In line with the idea of a pan-European product, EIOPA has a great role in ensuring a consistent application of the PEPP Regulation and the high-quality PEPP features. To that end, EIOPA is expected to scrutinise the PEPP market for any PEPPs that do not fulfil the requirements of the PEPP framework – and potentially raise significant concerns regarding consumer protection or pose a threat to the orderly functioning of the market. In line with Regulation (EU) No 1094/2010¹, EIOPA can (temporarily) restrict or prohibit the marketing, distribution or sale of certain PEPPs.

EIOPA has to provide technical advice to the Commission with regard to the adoption of delegated acts pursuant to Article 65(9) of the PEPP Regulation, specifying the criteria and factors to be applied by EIOPA when determining whether there is a significant PEPP saver protection concern or a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union. The development of those factors and criteria will also feed back to EIOPA's obligation to issue an opinion in accordance with Article 64(2) of the PEPP Regulation when competent authorities take measures to prohibit or restrict marketing or distribution of certain PEPPs.

Assessment and conclusion

The technical advice for specifying the criteria and factors for the product intervention powers under the PEPP Regulation is based and builds on the criteria and factors for EIOPA's product intervention powers in Commission Delegated Regulation (EU) 2016/1904². The criteria and factors listed therein are applicable also to PEPPs, with necessary adaptations. This approach is aligned with the approach suggested by the Commission in the Request for technical advice.

Effective market monitoring in close cooperation with the competent authorities will be a pre-requisite for enforcing EIOPA's product intervention powers.

The PEPP Regulation provides a framework for EIOPA's product intervention powers and lays down the factors and criteria to be applied by EIOPA, in determining when there is a significant PEPP saver protection concern, or a threat

¹ Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC; OJ L 331, 15.12.2010, p. 48.

² Commission Delegated Regulation (EU) 2016/1904 of 14 July 2016 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council with regard to product intervention; OJ L 295, 29.10.2016, p. 11.

to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union. As set out in Article 65(9), factors and criteria include:

- the degree of complexity of the PEPP and the relation to the type of PEPP saver to whom it is marketed and sold;
- the degree of innovation of a PEPP; an activity or practice;
- the leverage of a PEPP or practice;
- in relation to the orderly functioning and integrity of financial markets, the size or the total amount of accumulated capital of the PEPP.

A possible structure in the delegated acts could be to aggregate factors and criteria in major groups, following a logical sequence:

- PEPP product: factors and criteria (a) to (g);
- PEPP saver: factors and criteria (h);
- PEPP provider and PEPP distributor: factors and criteria (i) and (j);
- the size of potential detriment and wider impact on markets: factors and criteria (k) to (r).

EIOPA is of the view that the factors and criteria set out in Article 65(9) are not exhaustive and that inclusion of other relevant and related factors should be considered, taking into account and building from experience related to product intervention powers in other areas, in particular under the PRIIPs Regulation. The inclusion of factors and criteria related to the PEPP provider and PEPP distributor is anchored on this principle. The specific situation and circumstances of the PEPP provider or PEPP distributor, including the financial situation, solvency and business situation is relevant in determining the existence of a significant PEPP saver protection concern as it can be the root cause of practices and activities that can lead to detrimental consequences. The inclusion of these factors and criteria also reflects the existing interlinkages between conduct of business and prudential risks.

EIOPA may determine the existence of a significant PEPP saver protection concern based on one or more factors and criteria, i.e. not all factors and criteria must be met for EIOPA to temporarily restrict or prohibit the marketing, distribution or sale of certain PEPPs with certain specified features. This principle is aligned with the provision set out in the second subparagraph of Article 1(1) of the Commission Delegated Regulation (EU) 2016/1904.

EIOPA considers as essential that product intervention powers are dynamic enough to enable EIOPA to deal with a range of different exceptional situations. Product intervention powers can be used, as a measure of last resort, where a significant PEPP saver protection concern, or a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union has materialised. In addition, product intervention powers must also have a preventive function and allow steps to be taken to address issues before they become widespread.

The powers should also be applied in a proportionate way and, consequently, the factors and criteria to be assessed by EIOPA must remain flexible. EIOPA should be able to intervene in relation to new PEPPs that may not meet given criteria, or conversely not necessarily intervene if given criteria are met but overall consumer detriment or disorderly functioning of markets is not detected.”

The factors and criteria to be assessed by EIOPA to determine when there is a significant PEPP saver protection concern, including with regard to the long-term

retirement nature of the product, or a threat to the orderly functioning and integrity of financial markets or to the stability of whole or part of the financial system of the Union should be the following:

Factors and criteria related to the product

- (a) The degree of complexity of the PEPP, taking into account, in particular:
- the long-term retirement nature of the PEPP,
 - the type of underlying assets,
 - the complexity of the performance calculation, taking into account in particular whether the return is dependent on the performance of one or more underlying assets which are in turn affected by other factors,
 - the nature and scale of risks,
 - whether the PEPP is bundled with other products or services, or
 - the complexity of any terms and conditions;
- (b) The degree of transparency of the PEPP, taking into account, in particular:
- the type and degree of transparency of the underlying assets,
 - the degree of transparency of costs and charges associated with the PEPP,
 - the use of techniques drawing PEPP savers' attention but not necessarily reflecting the suitability or overall quality of the PEPP,
 - the nature of risks and transparency of risks,
 - the use of product names or terminology or other information that imply a greater level of security or return than those which are actually possible or likely, or which imply product features that do not exist, or
 - whether there was insufficient, or insufficiently reliable, information about the PEPP to enable market participants to which it was targeted to form their judgment, taking into account the nature and type of the PEPP;
- (c) The degree of innovation of the PEPP, an activity or a practice, taking into account, in particular:
- the degree of innovation related to the structure of the PEPP and its features, in particular the degree of innovation of the risk-mitigation techniques or of the type of decumulation options or of the design of other PEPP benefits,
 - the extent of innovation diffusion, including whether the PEPP is innovative for particular categories of PEPP savers,
 - innovation involving leverage, or
 - the past experience of the market with similar PEPPs or selling practices for PEPPs;
- (d) The particular characteristics or underlying assets of the PEPP, taking into account, in particular:
- the leverage inherent in the PEPP,
 - the leverage due to financing, or
 - the features of securities financing transactions;
- (e) The existence and degree of disparity between the expected return of the PEPP and the risk of loss, taking into account, in particular:
- the cost structure and other costs,
 - the disparity in relation to the provider's risk retained by the provider, or
 - the risk/return profile;

- (f) The pricing and associated costs of PEPP, taking into account, in particular:
- the use of hidden or secondary charges,
 - charges that do not reflect the level of service provided, or
 - the costs of guarantees or costs that do not reflect the actual cost or the fair value of the capital guarantee in case of a Basic PEPP;
- (g) The ease and cost with which the PEPP savers are able to make use of the switching portability services, taking into account, in particular:
- use of switching or portability services in relation to the phase in which the service is used, the fees and charges applied, or the loss of advantages and incentives,
 - the fact that the use of switching or portability service is not permitted or is made factually impossible, or
 - any other barriers;

Factors and criteria related to the PEPP saver

- (h) The type of PEPP savers to whom the PEPP is marketed or sold, taking into account, in particular:
- that the PEPP saver is a retail client, and not a professional client or eligible counterparty as defined in Directive 2014/65/EU³,
 - features characterising PEPP savers' skills and abilities, including the level of education, knowledge of and experience with other pension products, long term investment products or selling practices and the savers' vulnerability,
 - features characterising PEPP savers' economic situation, including their income, wealth and their degree of dependence on the PEPP for an adequate retirement income,
 - PEPP savers' core financial objectives, including pension savings and need for risk coverage, including biometric risks,
 - whether the PEPP is being sold to PEPP savers outside the intended target market, or whether the target market has not been adequately identified, or
 - the eligibility for coverage by a national guarantee scheme, where such schemes exist;

Factors and criteria related to the PEPP provider and PEPP distributor

- (i) The specific situation and circumstances of the PEPP provider or PEPP distributor, taking into account, in particular:
- its financial situation and solvency,
 - its financial activities or financial practices,
 - its business model, including its sustainability and transparency,
 - the suitability of reinsurance and guarantee arrangements regarding the PEPP, or
 - the PEPP provider's reliance on third parties for important features of the PEPP, such as coverage of biometric risks, guarantees and the portability of the PEPP;

³ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

- (j) The selling practices associated with the PEPP, taking into account, in particular:
- the communication and distribution channels used,
 - the information, marketing or other promotional material, or
 - the degree of innovation related to the distribution model, the length of the intermediation chain or the reliance on innovative techniques for the distribution model;

Factors and criteria related to the size of potential detriment and wider impact on markets

- (k) The size of potential detrimental consequences from the perspective of the individual PEPP saver and in case of a large number of current and potential PEPP savers , the potential detrimental consequences for a cluster of PEPP savers, taking into account, in particular:
- the size and total amount of accumulated capital of the PEPP,
 - the notional value of the PEPP,
 - the probability, scale and nature of any detriment, including the amount of loss potentially suffered,
 - the anticipated duration of the detrimental consequences,
 - the volume of the contributions,
 - the number and the fit and proper requirements of intermediaries involved,
 - the growth of the market or sales,
 - the average amount invested by each PEPP saver in the PEPP,
 - the coverage level defined in national insurance guarantee schemes law, where such scheme exist, or
 - the value of the technical provisions with respect to the PEPPs;
- (l) Whether the underlying assets of the PEPP pose a high risk to the performance of transactions entered into by participants or PEPP savers in the relevant market;
- (m) Whether the characteristics of the PEPP make it particularly susceptible to being used for the purposes of financial crime, in particular whether those characteristics could potentially encourage the use of the PEPP for:
- any fraud or dishonesty,
 - misconduct in, or misuse of information in relation to a financial market,
 - handling the proceeds of crime,
 - the financing of terrorism, or
 - facilitating money laundering;
- (n) Whether financial activities or financial practices of the PEPP provider or PEPP distributor in relation to the PEPP pose a particularly high risk to the resilience or smooth operation of markets;
- (o) Whether the PEPP or the financial activities or financial practices of the PEPP provider or PEPP distributor in relation to the PEPP could lead to a significant and artificial disparity between prices of a derivative and those in the underlying market;
- (p) Whether the PEPP or the financial activities or financial practices of the PEPP provider or PEPP distributor in relation to the PEPP pose a high risk to the

market or payment systems infrastructure, including trading, clearing and settlement systems;

- (q) Whether the PEPP or the financial activities or financial practices of the PEPP provider or PEPP distributor in relation to the PEPP may threaten PEPP savers' confidence in the financial system; or
- (r) Whether the PEPP or the financial activities or financial practices of the PEPP provider or PEPP distributor in relation to the PEPP pose a high risk of disruption to financial institutions deemed to be important to the financial system of the Union.