

# PROTECTION MECHANISMS FOR CONSUMERS IN THE PEPP.

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The PEPP regulation is the first Regulation aimed directly at consumer protection. This makes one wonder about the relationship with EU consumer law and its main principles. This paper will demonstrate that although legislators did not intentionally include the main principles of EU consumer law, three of them are present in effect.

PEPP Regulation – EU consumer law – consumer protection

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## Introduction

On the 29<sup>th</sup> of June 2017 the European Commission proposed a Regulation that would soon be known as the flagship of the Capital Markets Union: the PEPP.<sup>95</sup> After a turbulent legislative route through Parliament and Council, it came into force in the summer of 2019.<sup>96</sup>

The PEPP, unique in its kind, delivers an European answer to the changing demographics and economic situation of the European continent, recognizing the enshrined right to a life in dignity after retirement, as stipulated in article 25 of the EU Charter of Fundamental Rights.<sup>97</sup> Within the CMU action plan, it became the first initiative aimed at the consumer instead of financial services providers.<sup>98</sup> Rather, it created an opt-in regime that establishes minimum consumer safeguards to protect consumers against overly pricy retirement products and empower them to make informed choices via information requirements and

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<sup>95</sup> Regulation (EU) 2019/1238 of the European Parliament and of the Council of 20 June 2019 on a pan-European Personal Pension Product, OJ L 198, 25.7.2019, p. 1–63.

<sup>96</sup> August 14, 2019 to be precise. See article 74 of the PEPP Regulation.

<sup>97</sup> The charter can be consulted by accessing the following link: [https://www.europarl.europa.eu/charter/pdf/text\\_en.pdf](https://www.europarl.europa.eu/charter/pdf/text_en.pdf).

<sup>98</sup> Although the CMU is an appealing topic to explore, it would take us too far to elaborate on. We therefore gladly redirect the reader to the following article in the Journal of Financial Regulation: Demertzis, M., Merler S. Wolff G.B., Capital Markets Union and the Fintech Opportunity, *Journal of Financial Regulation*, Volume 4, Issue 1, March 2018, Pages 157–165.

mandatory advice. In that sense, the PEPP could be regarded as much of a consumer protection Regulation as part of the Capital Market Union.<sup>99</sup>

Provisions as to how to protect the consumer against providers is the subject of consumer law. Generally put, European consumer law has 2 purposes: First, to protect the weaker position of the consumer against the provider by for instance drawing up requirements of information and means of remedies. The second purpose was added more recently and consists of expanding the internal market by drawing up measures of protection.<sup>100</sup> A similar view can be found in the PEPP: Via requirements to protect the PEPP saver from ill-information it seeks to activate the PEPP saver to both ensure ‘good practices’ and expanding the internal market for pan- European individual personal pension products.

Now the correlation between the field of European consumer law and the PEPPR has been established, the question as to if and, if so how main principles from European consumer law are actually embedded into the PEPPR deserves attention. After all, the PEPPR foresees in consumer protection mechanisms in order to increase the internal market for individual pensions, but how does it relate to the principles of European consumer law?

This paper will examine whether the PEPP Regulation has incorporated main European principles with regard to consumer protection.

It consists of four parts: The first part will elaborate on the main principles of European consumer protection. The second part will present a selected overview of PEPP measures to illustrate how consumer protection is envisaged. In the third part, an analysis between the main principles as listed in part one and the measures as described in part two will be made. The paper will end with a conclusion.

An important note to make at this point is that legislative history reveals no indications as to intending to incorporate the principles of EU consumer law as stipulated in article 169 TFEU as a goal on its own.<sup>101</sup> That does not imply however, that these principles aren’t reflected in the provisions.

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<sup>99</sup> Recitals 31, 72, 81 and 89.

<sup>100</sup> European consumer law is a broadly covered topic. A reference to its historic purposes and dynamics can be found in the exhaustive works of Prof. mr. E.H. Hondius. For instance: Hondius, E.H., *Consumentenrecht*, Monografieën BW, A8, Kluwer, Deventer, 2013 (p.8-12). Another author worthwhile to mention is, Prof. mr. J.G.J. Rinkes. He has written a chapter on European consumer law in the following book: Hondius, E.H., G.J. Rijken (ed.), *Handboek Consumentenrecht*, uitgeverij Paris, derde druk, Zutphen, 2011, (p. 29-65). For references in English, German and French, we advise the bibliography attached to the following article of E.H. Hondius: Hondius, E.H., *Kroniek van het consumentenrecht*, NJB, March 10 1995, p. 388-395. Although the article stems from 1995, the sources are used and updated in more recent books and articles.

<sup>101</sup> More information about the legislative history of the PEPP regulation can be retrieved on the website of the European Commission: [https://ec.europa.eu/info/law/pan-european-personal-pension-product-pepp-regulation-2019-1238/legislative-history\\_en](https://ec.europa.eu/info/law/pan-european-personal-pension-product-pepp-regulation-2019-1238/legislative-history_en).

The object of research thus is to determine whether the PEPPR has envisaged the main principles of European consumer law. As a method of research these main principles will be mirrored in the Regulation. By means of comparison a possible link will be sought.

### **Part 1: The main principles of European consumer law**

In 1975 the European Council, inspired by developments that took place in the United States, adopted a Resolution which contained 5 fundamental rights of the consumer.<sup>102</sup> These rights function as main guiding principles in European legislation, and are codified in article 169 TFEU.<sup>103</sup> In order to ensure and promote a high level of consumer protection, protection measures on the following topics are to be held into account:

- Protection of health,
- Protection of safety,
- Economic interest,
- Information and education and
- Organization of means in order to ensure entitlement of consumer interests.

Other legal grounds can be found in the following sources: Article 38 of the Charter of Fundamental rights of the European Union which confirms the importance of consumer protection as well as articles 4(2)(f) and 114(3) TFEU.

Article 114 TFEU indicates that in proposals related to health, safety, environment protection and consumer protection the Commission will take as a point of departure a high level of consumer protection. In view of consumer protection, it complements article 169 TFEU. The latter also allow member states to introduce or maintain more stringent rules provided they are in accordance with the treaties. Article 12 TFEU clarifies that the notion of consumer protection should be taken into account in event of defining and implementing other policies.

This body of law, safeguards the main fundamental rights of consumers in the European Union. In the next part, the measures of consumer protection in the PEPP Regulation will be highlighted.

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<sup>102</sup> Council Resolution of 14 April 1975 on a preliminary programme of the European Economic Community for a consumer protection and information policy, *OJ C 92*, 25.4.1975, p. 1–1.

<sup>103</sup> Article 169 TFEU (1) reads as follow: “In order to promote the interests of consumers and to ensure a high level of consumer protection, the Union shall contribute to protecting the health, safety and economic interests of consumers, as well as to promoting their right to information, education and to organize themselves in order to safeguard their interests.”.

## **Part 2: PEPP Measures and consumer protection**

As has been established in the previous paragraph, there are five main principles that govern European consumer protection law. This paragraph will examine how these principles are represented in the PEPP Regulation.

Clear and concrete examples are the transparency on costs and fees and a cost-cap for the Basic PEPP, the need to provide advice and information, the portability and the possibility for consumers to lodge complaints against providers at the national supervisory authorities of their Member State of residence.

### **Fee-cap and portability**

The PEPP features a cap on the costs and fees for the Basic, or default option. Set at 1%, this cap protects the PEPP consumer from overpriced products and limits the investment options to simple strategies. The general thought behind this cap is that for average (financial illiterate) consumer<sup>104</sup>, a key focus should be on (i) value for money and (ii) simplicity of the product. Even though objection against these goals itself is hard, stakeholders objected against the stringent level of the fee-cap, allegedly rendering the PEPP commercially unviable.<sup>105</sup> During the initial discussion of the draft PEPP Regulation, some experts warned that there is no clear evidence that the proposed PEPP framework will lead to increase in the retirement savings.<sup>106</sup> However, consumer organizations welcomed the fee-cap as pension products often underperform and suffer from high costs.<sup>107</sup> The Basic PEPP however, features more measures to protect the consumer.

The default option has, besides maximized fees also limited investment choices. As the goal of the Basic PEPP is to provide a form of capital protection<sup>108</sup>, the default option has to make use of either a life-cycle strategy or a be based on a capital guarantee.<sup>109</sup>

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<sup>104</sup> The PEPP actively promotes financial literacy education in recital 18.

<sup>105</sup> Lannoo, K. 2019. "Ceci n'est pas un PEPP," ECMI Papers 494, Centre for European Policy Studies

<sup>106</sup> Dimitrov St., (2017). "The PEPP Regulation and its influence on the Bulgarian market of insurance", ISBN 978-954-8590-45-7, VUZF Publishing House, Sofia, 2017, pp. 40 - 49

<sup>107</sup> Better Finance, Pension Savings The Real Return, 2019. See also a press release by EFAMA, EFAMA welcomes the European Parliament's approval of the trilogue agreement on the PEPP, 2019.

<sup>108</sup> See also article 37 of the PEPP proposal; Proposal for a Regulation of the European Parliament and of the Council on a pan-European Personal Pension Product (PEPP), 2017/0143(COD).

<sup>109</sup> For an overview, see the Working Document on the proposal for a regulation of the European Parliament and of the Council on a pan-European Personal Pension Product (PEPP) of 29 11 2017, (COM(2017/0343 - C8 4393/2016 - 2017/0143(COD)); in 't Veld S., Het Pan-Europees Persoonlijk Pensioenproduct: een Super Rubik's Kubus, PensioenMagazine 2018/76, J.J. van Zanden 'the PEPP', in: H. van Meerten, *EU pension Law*, Amsterdam University Press: 2019.

Possibilities under the PEPP, at least for the default option seem to be limited to ensure that the PEPP is ‘safe’, in line with the objective to at least recoup the capital invested.<sup>110</sup> In other words, the default option has to be in the ‘economic interest’ of the PEPP saver. However the possibility of choice might also be in the best economic interest of the consumer– taking a more consumer centric point of view.

This split between both limitations on the default and the possibility to take (more risky / complex) alternative investment options within the PEPP seems to try to make a compromise between both allowing providers to innovate and come up with suitable products, as to protect consumers from unsuitable products.

Portability plays an important role in the PEPP Regulation, not only as a manifestation of the free movement of services and the possibility to ‘stay in their product’ when moving to another Member State, but also as the right to switch PEPP providers (articles 52 - 56). This flexibility and individual choice can be considered as a part of the economic interest of the consumer; if a product is underperforming or other providers offer better conditions it is in the consumers interest to not be stuck-in-plan.

To that extent, the portability and flexibility of the PEPP may be seen as a contra weight to the restriction of the Basic PEPP. From a consumer interest perspective, the PEPP clearly chose to prevent providers from offering unsuitable products to a PEPP saver, both through a negative and positive protection.

### **Information requirements**

The right to information and education is an important element of the acquis of consumer protection law and is very clearly reflected in the PEPP Regulation.

Besides the restrictions on the product itself, in particular the Basic PEPP, the PEPP features a heavy informational regime which was inspired by both the PRIIPs<sup>111</sup> and the IORP<sup>112</sup> and sets rules for information pre-contractual, at time of contract, annual, pre-retirement and information after retirement.<sup>113</sup> Besides this informational regime, the provision of the PEPP is also subject to very detailed advice, included a personalized assessment of the demands and needs of an individual PEPP saver.

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<sup>110</sup> Recital 54.

<sup>111</sup> Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs)

<sup>112</sup> Directive (EU) 2016/2341 of the European Parliament and of the Council of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs)

<sup>113</sup> See Chapter VI of the PEPP Regulation.

Combined, the PEPP offers the strictest informational regime out of the European legislation. Especially the mandatory and personalized advice is a one-of-its-kind measure. From a consumer protection point of view, it might be a little too much, considering that the aim of the Regulation was to create a simple, value for money product.<sup>114</sup> It can be argued that once the product is indeed safe and simple, the informational regime should reflect that objective. However, as the PEPP is a retirement product with a very long investment horizon and a consumer might want to be well informed before purchasing a (potentially costly) product that will only pay out after 40 years mandatory advice might add to consumer protection.

One of the main concepts of the PEPP is that it doesn't interfere with national rules governing the decumulation period to safeguard the division of competences. Taxes are, after all a Member State competence. The way outpayments are incentivized differs between Member States as well, however choices made concerning them do affect the PEPP saver greatly. A lump sum or an annuity as a way of outpayment makes a great difference in both spending power as in the existence of a steady income. For this reason, the PEPP introduces the 'wakeup call' in article 60 to help the consumer with planning for retirement. Due to this ongoing obligation to inform the consumer, the PEPP has a heavy emphasis on the right of information as stipulated in article 169 of the TFEU.

### **The complaints procedure**

As the PEPP is a complex and long-term product, an effective conflict resolution is important and considered one of the key elements of consumer protection. The PEPP, as an individual product, opens the possibility for collective complaint procedures before court or via alternative dispute resolution. Aimed at cross-border workers and in light of the internal market, PEPP consumers are allowed to lodge their complaints at the national supervisor of the Member State of residence, regardless of where the infringement occurred.<sup>115</sup> This option solidifies the third principle mentioned under part 1: Organization of means in order to ensure entitlement of consumer interests.

## **Part 3: Consumer protection – how much is too much?**

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<sup>114</sup> In the original proposal of the Commission, the aim of having a default option was to prevent the need of advice. However, during the political process this changed due to different views on investment options and ways to protect the consumer.

<sup>115</sup> Rightfully considered as consumer protection measures by the Rapporteur Sophie in 't Veld in: S. in 't Veld, Het Pan-Europees Persoonlijk Pensioenproduct: een Super Rubik's Kubus, PensioenMagazine 2018/76 p. 4.

As for the principles of protection of health and safety, the PEPPR does not contain provisions.

This is to be explained by the fact that the PEPPR aims at laying down uniform rules on the registration, manufacturing, distribution and supervision of PEPPS that are distributed in the Union.<sup>116</sup>

As for of the principle of economic interest, information, education and organization of safeguarding entitlement concerning the PEPPR does provide provisions. The economic interest of the consumer plays a major role in the PEPP Regulation. One of the key aspects is the fee-cap for the Basic PEPP – obligating providers to offer a simple and cheap product as a default. Installing a fee-cap can be seen as an effective way to safeguard the consumers economic interest. However, setting the cap too low will discourage providers to offer the PEPP at all, which renders its protection useless and impacts consumers choice. The PEPP Regulation establishes a European label of safety and quality, a first for a financial product. However, that entails that the PEPP needs to live up to expectation and results in a debate on what safety of a financial product is. To that extent, consumer protection is an important element which takes into account the increasing individual responsibility<sup>117</sup> of a saver. The measures of the PEPP mainly focus on preventing losing money for the consumer, which is an understandable point of view from a policy perspective. Faulty PEPPs would not only damage consumers, but the image of Europe as well. In this quest for safety, economic interest of the consumer has acquired a central role. However, by regulating and restricting the product, at least for the Basic PEPP also leads to the question on *why* advice is *mandatory* as well. As a balance, one might argue that since the product is ‘safe’, a consumer looking into purchasing a product isn’t necessarily better protected by adding mandatory, personalized (and expensive) advice. Rather, the rationale behind mandatory advice is to prevent the consumer from buying unsuitable products, even if the consumer opts for the default option which is, according to the wording of the Regulation “safe” (article 45). Furthermore, apart from the fee-cap and advice, the PEPP Regulation has an extensive informational regime which provides the consumer with both pre-contractual and ongoing information during accumulation and decumulation. Economic interest and informational requirements are strongly developed in the PEPP Regulation, but perhaps counteract rather than complement each other.

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<sup>116</sup> Article 1 of the PEPP Regulation.

<sup>117</sup> Dimitrov, St. (2018). “Adequate and sustainable pensions - where is the balance between pay-as-you-go public pensions and capital pensions”, p.62, VUZF Review, vol. 3, 2018, pp.57-67, ISSN: 2534-9228

In article 50 of the Regulation, a complaints procedure is set into place. Through this procedure it is settled that PEPP savers are able to lodge a complaint to ensure their rights and obligations under the Regulation. The information as where to, and the language of the procedure shall be either in an official language of the European Union or unless agreed otherwise between the PEPP saver and the distributor in another language. The Regulation stipulates that in terms of requirements otherwise than language, should be “clear, comprehensive and easily accessible”.

This also applies to the general terms and conditions of the contract between the PEPP provider and the saver. Furthermore distributors are kept to make every possible effort to reply, either electronically or in another durable medium. Finally, the PEPP provider has to direct the PEPP saver to at least one alternative dispute resolution (ADR) body which is competent to deal with disputes.<sup>118</sup> The exact wording in the article concerning ADR is: “shall inform”.<sup>119</sup> If one interprets this as an obligation, it is a decent step forward for the PEPP saver to ensure consumer protection. An ADR is an autonomous, private body that produces dispute regulation. So when this is a default part of a contract, at least the saver has the presence of an independent body to rule a conflict.<sup>120</sup> The actual impact of this inclusion however does depend on the chosen tool of the provider in the contract. This could be going from simple mediation binding advice.

#### **Part 4: Conclusion**

The PEPP was launched as the flagship of the Capital Markets Union; aiming to provide European citizens with a safe way to invest for retirement as well as opening up the internal market for individual pension products. The PEPP is in essence a consumer protection Regulation; protecting the consumer in its weaker position in comparison to the provider, as well as establishing safeguards to encourage participation in the internal market. EU consumer law is based on 5 principles: Protection of health, Protection of safety, Economic interest, Information and education and Organization of means in order to ensure entitlement of consumer interests.

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<sup>118</sup> It would bring us too far to discuss the place of an ADR body within the structure of regulation of rights. An example of an ADR body in the Netherlands is the Netherlands Arbitration Institute (NAI). Providers may include a clause in their contract that in case of a dispute, the dispute will be concluded by a decision of the board. For more information, see the NAI (<https://www.nai-nl.org/en/>). See also: Meijer (G.J.) and Snijders (H.J.), *Vademecum Burgerlijk Procesrecht. Arbitrage*, Kluwer, Deventer, 2002.

<sup>119</sup> Article 50 (4) of the Regulation.



The PEPP Regulation contains references to the main principles of European consumer law on 3 points: economic interest, information and education and organization of safeguarding entitlement.

Via the Basic PEPP and its cost cap of 1%, the consumer is protected against overly priced products. Furthermore, by installing mandatory personalized advice the Regulation tries to prevent a mismatch between consumer and product. The PEPP features an extensive regime covering informational requirements – including a wake-up call when the product reaches the decumulation phase.

In its quest to protect the consumer, installing both a fee-cap of 1% and having mandatory advice might be contradictory. After all, if a Basic PEPP is already regulated so strictly, one might assume it's a safe product suitable for most PEPP savers. If advice is mandatory, the Basic version could be regulated less strictly as personalized advice would be provided anyway.

The possibility of lodging complaints at the national supervisor of Member State of residence is a good step towards consumer protection, empowering the consumer to take action against non-performing providers.

Albeit not perfect, the PEPP is a welcome step in the protection of pension consumers and in the establishment of an internal pensions market.

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