

Chapter 2

Scope rules under article 4A of the PRIIPs Regulation

2.2 Scope rules

General distinction between PRIIP and non-PRIIP debt securities

2.2.1

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- (1) A *debt security* is not a PRIIP if it meets the following criteria:
- (a) it does not fall within ■ DISC 2.2.2R;
 - (b) the *issuer's* default risk is wholly or predominantly determined by the economic performance of the commercial or industrial activities of the *issuer* (or, where the *debt security* is guaranteed by a *group person*, that *person*); and
 - (c) the terms of the *debt security* do not impose any modification, structuring, or conditionality on the *issuer's* obligation to pay interest or repay the principal save for the effect of any feature listed under ■ DISC 2.2.4R.
- (2) For the purposes of (1)(b), lending, investment, and any other financial sector activities are not commercial or industrial activities.

2.2.2

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- (1) A *debt security* is a PRIIP where the level of interest payable, any conditionality of principal repayment, or the *issuer's* default risk, is linked to or materially dependent on the following, whether or not modified by a pre-determined formula:
- (a) fluctuations in reference indices or benchmarks relating to investment assets or a class of investment assets, for example a stock market index;
 - (b) the value or performance of reference investment assets, such as a basket of *shares* or specified *commodities*; or
 - (c) the value or performance of *investments* held by the *issuer* (or by a *person* connected to the *issuer*).
- (2) For avoidance of doubt, the following are excluded from (1)(a):
- (a) the Bank of England official Bank Rate; and
 - (b) any benchmarks or indices tracking the rate of inflation, money market interest rates, or other indicators pertaining to the performance of the general economy.

2.2.3

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In ■ DISC 2.2.2R(1)(c):

the *investments* include, for example, *derivatives*, real estate holdings, a pool of receivables, or a portfolio of *securities*; and

a person is connected to the *issuer* if it is a member of the same group as the *issuer*, has a relevant business relationship with the *issuer*, or otherwise does not have an arm's-length relationship with the *issuer*.

Neutral features

2.2.4

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The following features do not cause a *debt security* to meet the criteria for a PRIIP in article 4(1) of the *PRIIPs Regulation*:

- (1) a fixed *coupon* rate, including where:
 - (a) a set *coupon* rate applies until maturity, including a nil or zero rate; and
 - (b) the *coupon* rate is subject to pre-defined changes at fixed times prior to maturity – that is, a stepped *coupon*;
- (2) a floating or variable *coupon*, provided that:
 - (a) the interest payable is determined by an index or benchmark of the kind described by ■ DISC 2.2.2R(2), with or without a spread reflecting the credit risk of the *issuer*; and
 - (b) the interest payable is not subject to any additional modification or structuring such as, for example, a cap, or a floor other than zero;
- (3) a put *option* giving the investor a discretion to demand early repayment of the *debt security* on pre-agreed terms, or giving the investor the choice to convert or exchange their *debt security* into one or more *shares* of the same *issuer* at a pre-determined price;
- (4) a call *option* allowing the *issuer* to redeem a *debt security* early at a price higher than or equal to par, where:
 - (a) the *option* becomes exercisable due to changes in the financial health, market confidence in, or control of, the *issuer*, or general economic conditions, but not including *options* exercisable in response to fluctuations, price movements or performance of an index, benchmark, specified asset or underlying asset falling within ■ DISC 2.2.2R(1); and
 - (b) the mechanism to calculate the net present value of the future *coupon* payments is made clear to the investor in the terms of the *debt security*;
- (5) a perpetual or indefinite term; or
- (6) the *debt security's* subordination in the creditor hierarchy in the event of the *issuer's* insolvency.

Legacy products traded on secondary markets

2.2.5

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A financial instrument issued prior to 1 January 2018 is not a PRIIP.