



EUROPEAN COMMISSION
HEALTH & CONSUMER PROTECTION DIRECTORATE-GENERAL
Directorate B - Consumer Affairs
B5 - Financial services

SUMMARY DOCUMENT

1. Background

Council Directive 87/102/EEC on consumer credit¹, amended in 1990 and in 1998², was based on a Commission proposal put forward in 1979 and established the Community framework for consumer credit in order to contribute to the creation of a common market in credit and to introduce minimum common rules on consumer protection.

The Commission in 1995 submitted reports on the implementation of this Directive³, and subsequently undertook a broad consultation of the interested parties. In 1997, it put forward a summary report on the reactions and comments to the 1995 report⁴.

This prompted the Commission to conclude that the Directive was no longer sufficiently in step with the situation of the consumer credit market and that it should therefore be revised⁵.

The Commission accordingly ordered a series of studies on a range of specific issues⁶ and carried out a detailed comparative analysis of all national transposal legislation.

An analysis of the European frontier-free market in consumer credit shows that there has been only marginal growth in this market.

As a result, the legal framework currently in force needs to be reviewed in order to allow consumers and companies to take full advantage of the single market.

2. Guidelines for the draft revision of Directive 87/102/EEC

The low degree of development of the cross-border credit market in Europe is explained by a number of factors, the main ones being:

- the technical difficulties of penetrating another market,
- the lack of sufficient harmonisation of national legislation,
- and the developments in techniques and forms of credit since the Directive was submitted by the Commission and adopted by the Council.

The revision of the Directive requires:

- adaptation of the legal framework to the new credit techniques,
- rebalancing of the rights and obligations of credit consumers and credit grantors alike,
- a high level of consumer protection.

The aim is to promote the development of a more transparent, more effective market providing a high enough degree of consumer protection so that the freedom of movement of credit can take place in better conditions for both supply and demand.

The relevant Commission departments would like to put forward the guidelines for the revision they intend to propose and consult the Member States and the interested circles on the main approaches of the text, highlighting in certain cases the options they consider to be the most relevant.

In order to achieve these objectives, the revision of the Directive would be carried out applying the following six guidelines:

- (1) redefinition of the Directive's scope in order to adapt it to the new market situation in this area and better tracking of the demarcation line between consumer credit and real estate credit;
- (2) inclusion of new arrangements taking account not only of the creditors but also of credit intermediaries;
- (3) introduction of a structured information framework for the credit grantor in order to allow him to better appreciate the risks involved;
- (4) more comprehensive information for the consumer and any guarantors;
- (5) more equitable sharing of responsibilities between the consumer and the professional;
- (6) improvement of the arrangements and practices for processing payment incidents by the professionals, both for the consumer and for the credit grantor.

3. The purpose of the consultation

The Commission's intention is more specifically to consult the Member States and the interested circles on:

- *whether there is a case for extending the scope of the Directive, in particular to henceforth cover credit secured by a mortgage but intended to finance the purchase of consumer goods or services;*
- *what should be done to improve information to the credit grantor, in full respect of existing rules with regard to the protection of data on private life. In particular, there should be an examination of whether steps should be taken to encourage the use of:*
 - *“negative” national databases recording default of payment;*
 - *“positive” national databases, i.e. recording all the consumer's credit commitments;*
 - *national databases, both negative and positive.*
- *whether the rules set out in Directive 87/102 on the joint and several liability of the seller of goods and services and the credit grantor should be amended;*

- *lastly, whether action needs to be taken on insurance to cover certain risks of default of payment. In particular, the merits of a mechanism based on individual insurance or a — compulsory — portfolio insurance for the credit grantor should be discussed.*

The achievement of these objectives would involve contemplating moving on from minimum harmonisation to maximum and optimal harmonisation which would guarantee a high level of consumer protection across the whole of the European Union.

Discussion paper for the amendment of Directive 87/102/EEC concerning consumer credit

THE SITUATION

The primary aim of Directive 87/102/EEC and its two revisions was the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit, in order to contribute to the creation of a common market in the area of credit and to introduce minimum common rules for consumer protection⁷.

When these Directives were transposed⁸, the Member States felt that the level of protection they offered was inadequate, an observation which resulted on the one hand in a clear resolve to improve consumer information and protection and, on the other, consideration of the types of credit and/or new forms of credit contracts which were not covered by these Directives⁹. This attitude, which was widespread throughout Europe, gave rise to a broad application of the minimum clause by the Member States¹⁰.

Credit techniques have since then evolved considerably and the Directive today seems out of step with these trends.

Another point is that there has so far been only marginal growth in the European consumer credit market.

According to the 1995, the Commission feels that the legal framework currently in place should be reviewed in order to allow consumers and companies to take full advantage of the single market. The aim is to allow genuine freedom of movement for credit through the development of a more transparent, more effective market offering a high degree of consumer protection and the opportunity for professionals to better appreciate the risks involved.

A review of this kind requires the adaptation of the legal framework to the new credit techniques. It entails rebalancing the rights and obligations of credit consumers and credit grantors alike.

The Commission accordingly feels that the revision of the Directive should be conducted in accordance with the following six guidelines:

- (1) redefinition of the Directive's scope in order to adapt it to the new market situation in this area and better tracking of the demarcation line between consumer credit and real estate credit;
- (2) inclusion of new arrangements taking account not only of the creditors but also of credit intermediaries;
- (3) introduction of a structured information framework for the credit grantor in order to allow him to better appreciate the risks involved;
- (4) more comprehensive information for the consumer and any guarantors;

- (5) more equitable sharing of responsibilities between the consumer and the professional;
- (6) improvement of the arrangements and practices for processing payment incidents by the professionals, both for the consumer and for the credit grantor.

Lastly, the achievement of these objectives would involve moving on from minimum harmonisation to maximum harmonisation which would guarantee a high level of consumer protection across the whole of the European Union.

1. REDEFINITION OF THE SCOPE OF THE DIRECTIVE

1.1. Definition of consumer

Directive 87/102/EEC defines the consumer as “*a natural person who, in transactions covered by this Directive, is acting for purposes which can be regarded as outside his trade or profession*”¹¹.

Question 1.1:

In view of the different definitions¹² adopted by certain Member States, is there not a case for extending this definition to natural persons — whether self-employed or in paid employment — who use consumer credit for professional purposes?

If the answer to this is yes, the options are as follows:

1.1.1 The definition should be amended to include: on the one hand, associations of natural persons and, on the other, natural persons who wish to set up in business.

1.1.2 The definition should be amended in order to cover mixed contracts, i.e. credit contracts granted to a natural person for purposes which are mainly, but not exclusively, private¹³.

1.2. Credit contracts covered by the Directive

Article 2 of Directive 87/102/EEC lists a series of exemptions which today appear to be no longer justified. The new Directive would apply to all forms of credit granted to natural persons for mainly private purposes:

- irrespective of the amount,
- irrespective of the security required,
- and irrespective of the purpose of the credit¹⁴, with the exception of that intended to finance the purchase or renovation of buildings¹⁵.

It should be noted that:

a) the difference between the “consumer credit” market and the market in “real estate credit” and “mortgage-backed credit” is becoming increasingly small. The financial techniques used have become virtually identical: fixed or variable rate, the option of one or several instalments, regular periods or reimbursement at the end of the contract, straight loan or opening of a credit line, mortgage registration, guarantee, etc.;

b) the mortgage is being increasingly used thanks to mortgage techniques which cover all types of credit in the area of funding of the purchase of consumer goods. This trend involves serious potential risks for the consumer whenever he/she uses his/her home as collateral to guarantee consumer requirements, in the same way as the “equity release” techniques in the United Kingdom. A mortgage can in several Member States, be dissociated from all credit debts and be of undetermined duration¹⁶. Credit accompanied by mortgage registration as second (or even third or fourth) charge is also used in many instances to refinance consumer credit. There would therefore seem to be no longer any

reason to maintain an artificial distinction between “consumer credit” and “mortgage credit”.

Questions 1.2:

The following questions need to be considered:

1.2.1 As regards the exemptions listed in the current Directive concerning thresholds and ceilings¹⁷, interest-free credit, hiring to finance the utilisation of goods and services, consumer credit established by authenticated act, etc. is there a case for doing away with these?

N.B. Every party consulted wishing to propose the maintenance or introduction of an exemption is urged to justify it.

1.2.2 With regard to credit backed by a mortgage and real estate credit intended for housing, is there a case for making a distinction between the first and the second, and to do away with the exemption for credits backed by a mortgage not exclusively intended for a real estate transaction, in order to include these within the scope of the Directive?

1.2.3 Is there a case for dealing with real estate credit and housing loans, comprehensively or partly, in the context of the draft revision?

1.3. The annual percentage rate of charge (APR)

The annual percentage rate of charge (APR) is that rate which “on an annual basis, ... equalises the present value of all commitments (loans, repayments and charges, future or existing, agreed by the creditor and the borrower” (Article (1)(a) of the Directive. Two subjects need to be examined: the basis for calculating the APR and the calculation itself.

1.3.1. Basis of calculation of the APR

In theory, the APR must include all credit costs. Directives 90/88/EEC et 98/7/EC amending Directive 87/102/EEC provide for a negative list of costs which should be excluded from this basis of calculation. If the APR is to be fully reliable and usable throughout the European Union, ideally it should be calculated by the Member States in a uniform manner incorporating in the same way all the cost elements linked to the credit contract. Yet this is not always the case despite the amendments made by Directive 98/7/EC.

Generally speaking, the inclusion or exclusion of certain costs should be reevaluated on the basis of their economic justification¹⁸, so as to arrive at a minimum of exclusion of credit cost elements from the basis for calculation. This should bring about a genuine approximation of the national “bases of calculation” and a higher uniformity of calculation, thus enhancing transparency and comparability.

In actual fact, the problems encountered in proving the “compulsory” nature of insurances and securities covering reimbursement of the credit — this compulsory nature being the criteria for including their cost in the basis of calculation — have prompted certain Member States to regulate beyond the Directive by using the minimal clause. These countries felt that the consumer in practice had no freedom of choice and that the

lender, for reasons of caution or commercial profit, preferred to negotiate insurance right away, even if the consumer did not initially want such insurance¹⁹.

Question 1.3.1:

The following questions should be discussed²⁰:

- 1.3.1.a) should the costs arising from both personal security and real security be incorporated?
- 1.3.1.b) should certain factors such as taxes, commissions for credit intermediaries, etc. be specified?

1.3.2. Calculating the APR

Directive 98/7/EC leaves the choice between different time parameters, which leads to genuine imprecision in calculating the APR²¹. Moreover, there are no hard and fast rules as regards mixed financial products containing simultaneously a credit element and a savings or insurance element (life/mixed).

Question 1.3.2:

Is there a case for:

- a) on the one hand specifying and standardising this calculation by setting out examples covering each financial technique?
- b) and on the other, finding a common methodology for:
 - (i) integrating
 - (ii) or standardising
 - (iii) or neutralising these mixed elements?

1.4. Lending rate

The concept of “annual rate of interest” is used in Article 6 of Directive 87/102. This concept is not, however, defined. The fact is that when wanting to regulate current account advances, overdrafts, and therefore, more generally, all credit contracts for which the debit interest is calculated after the event, this rate should be defined both on an annual basis and on a periodical basis. The same rate should be able to be applied in all Member States in order to be able to compare statements, to check interest claimed for the period specified, etc.

Question 1.4:

- 1.4.a) Is a definition of the annual rate of interest necessary and,
- 1.4.b) should this rate be calculated using the same formula as that for the APR, and if necessary be converted using the equivalent conversion method^{22 23}?

2. CREDIT INTERMEDIARIES

Article 12(1) of Directive 87/102 offers Member States three options for monitoring the implementation of the Directive particularly as regards credit intermediaries. The report on the implementation of the Directive suggested making the third option listed in this article compulsory. This option stipulated that Member States must promote the establishment of appropriate bodies to receive complaints concerning credit agreements or credit conditions and to provide consumers with appropriate information or advice²⁴.

More stringent control of credit intermediaries entails a number of steps:

- registration of such persons,
- the creation of an access threshold in terms of professional aptitude,
- the option, where required, of suspending or withdrawing their licence,
- making any complaints public.

This implies that each Member State must register the sellers and/or distribution channels of credit agreements.

The best formula would be to make the three options listed in Article 12(1) of Directive 87/102, compulsory in a cumulative manner:

In the new Article 12 provision could be made for a common platform for all credit intermediaries, while still allowing differences as regards the quality and extent of the powers of the credit intermediary and even more so as regards the responsibility of the lender in relation to the intermediary selected or accepted (credit broker, delegated agent, seller).

Question 2:

2.1 Is the solution of making the options cumulative and allowing for differences acceptable?

Or should one or more of the following solutions be preferred:

2.2 Harmonising the conditions of access to the profession of credit intermediary, as regards the conditions of good repute but also professional aptitude.

2.2.a) If conditions of aptitude are applied, it is proposed that they be assimilated whenever possible to those laid down for insurance intermediaries.

2.2.b) Moreover, it would be advisable either to draft a special statute for “sellers” (by putting them under the responsibility of the lenders), or to exclude them from the profession given their established lack of “aptitude” to pursue an activity of this kind.

2.3 Ensure the provision of accurate information as regards the quality and extent of the powers of the credit intermediary, and the possible exclusive nature of his cooperation with the lender²⁵.

2.4 Mention the intervention of a credit intermediary in the agreement and make the identity of the credit intermediary compulsory. Details of the extent of their powers are linked to the problem of there being no definition of credit intermediary.

2.5.a) Ensure better transparency of the intermediary's remuneration, particularly by mentioning in the credit agreement any commissions to be paid, which should also be included in the APR^{26 27}.

2.5.b) Moreover, consideration could also be given to staggering the commission in order to encourage a responsible attitude in the intermediary with regard to credit agreements affected by payment defaults.

2.6.a) Lastly, is it acceptable for a credit intermediary to be authorised to make direct claims on the consumer for remuneration when credit or information is applied for or

2.6.b) is it advisable to opt for a total ban as provided for by certain Member States, bearing in mind that the system of staggering commission payments can be effective only subject to this condition?

3. IMPROVING INFORMATION FOR THE CREDIT GRANTOR

The cost of credit is a function of the risk for the lender, this risk itself being a function of the quality of the information available to the lender when deciding to enter into an agreement with the consumer.

The information to the lender is therefore essential as regards the operation of the credit market and particularly consumer credit.

The importance of the quality of this information is further heightened in the event of offering credit to consumers established in other Member States.

The improvement of information to the credit grantor is thus an essential condition for the creation of the internal consumer credit market, without which the consumer will find it very difficult to obtain credit in another Member State.

Negative records — recording payment defaults — and/or positive records — recording all the consumer's credit commitments — exist in all Member States. These records are either private or public.

Positive central records — public or private — exist in Germany, the Netherlands, Austria and the United Kingdom. Belgium will also be introducing one shortly. Agreements on exchanges between these central records agencies also exist, e.g. between Belgium and the Netherlands, or between Belgium and Germany.

Certain Member States²⁸ have placed the onus on the lender to assess and verify the consumer's solvency, *inter alia* with the help of a centralised database. This obligation reflects the concern to use a transparent and objective system of assessing the solvency of consumers and, where applicable, the guarantors.

Another point is that making such information systematic, subject to strict respect of the rules for protecting private data, would make it possible to avoid the situation whereby lenders use indirect means which are not so secure and offer no possible control by the consumer as regards the information concerning him, e.g. the use of electoral registers, or partial databases of private information.

The general interest also requires that the collection and processing of personal information on consumers be secured by transparent records functioning within a secure framework respecting the rules on privacy and which allow access to cross-border credit to all consumers, while preserving the certainty that those exposed to the risk of excessive indebtedness will no longer be accepted.

Question 3:

As part of the overall examination a number of questions based on different degrees of harmonisation can be envisaged:

The lender approved in one Member State must be able to have access in the same conditions to sources of information and databases in other Member States.

3.1 How can access by lenders to information on consumers be ensured?

3.2 Is there therefore a case for providing only adequate and objective information on consumers in every Member State or will the current situation suffice?

3.3 In the first hypothesis, what needs to be done to make sure that such information can be obtained:

3.3.a) Should the way in which data are collected be harmonised, the sole aim being to appreciate the solvency of the consumer or the guarantor?

3.3.b) Should it be specified that data cannot be communicated other than within the framework of this legitimate interest pursued by the person responsible for processing the data and on condition that they not be in contradiction with the interest or the rights and fundamental freedoms of the person concerned?

3.3.c) If the consumer gives information to a professional in order to obtain a credit, should he have the certainty that it is only within this framework alone that the data will be handled? Should it consequently be prohibited for the data to be collected, marketed, sold or stored by third parties who have no direct link with the consumer in the context of a credit transaction?

3.4.a) Should the idea of “responsible lending” be promoted, particularly by placing the onus on the credit grantors to appreciate and verify the solvency of the consumer, by consulting information which is neutral, reliable, independent and accessible to all lenders in the EU and to consumers with regard to the information relating to them?

3.4.b) If this idea of a “responsible lending” is accepted, should provision be made for rules whereby the consumer must answer questions put in a precise and comprehensive way, the onus of proving that they have asked the appropriate questions — if necessary by using a questionnaire — being on the lender and/or credit intermediary?

3.5 Should a common approach be based on records? If the need for a system based on records were confirmed, what type of record should be envisaged?

3.5.a) Should preference be given to negative databases?

3.5.b) Or on the contrary should positive records be established in all the Member States?

3.5.c) Or should both be kept?

The Commission is eager to receive the opinion of the various parties interested on the record which would appear to be the best solution for reaching a balance in relation to the various objectives set out above.

4. IMPROVING INFORMATION TO THE CONSUMER AND THE GUARANTORS

4.1. Better information for the consumer

Better information to the credit grantor goes hand in hand with better information to the consumer.

Transparency with regard to the conditions of credit supply is an essential element for better comparability of products on the market, including those originating in other Member States. It is the precondition for real free circulation of supply.

The Directive should apply to all credit contracts and should therefore be adapted in order to cover the new forms of credit which have emerged on the market since Directive 87/102/EEC was adopted.

Financial techniques nevertheless prevail over the typology of the credit agreement and it is therefore important to have provisions to supply first and foremost appropriate information for the consumer as a function of the techniques used.

This information should cover amongst other things:

- the interest rate: the consumer must be informed at least of the conditions under which this rate can vary, on how the rate is calculated, on the periods during which it will be applied, etc.;
- repayment arrangements: is the consumer to repay on a regular basis, in one go, by paying limited instalments for a certain period and a large sum at the end²⁹, in cash or in kind?
- withdrawing arrangements: can he/she draw on the sums made available once or several times, in a staggered or a repetitive way, is there a clean-up requirement, etc.?
- amortisation table: this should be given to the consumer for all contracts for which interest and charges are fixed and calculated beforehand.

Question 4.1:

Should Articles 3 (publicity), 4 and 6 (agreements in general, current account advances), be reworded in order to ensure sufficient information for the consumer with regard to all credit agreements?

4.2. Guarantors

The fate of people other than the consumer who stand as guarantors is a matter of concern to a number of Member States. These persons currently fall through the net of Directive 87/102/EEC³⁰.

On the one hand, the scope of the Directive should be extended and cover the guarantees annexed to credit agreements and the persons who provide them. On the other, the Directive should cover the case of people acting for a purpose which can be considered outside their commercial or professional activities and who are asked to provide a guarantee for a credit agreement not covered by the terms of this Directive. These

guarantors — for example, the parents of a businessman starting up in business — act as consumers and as such need information and protection identical to those they would receive if it were a consumer credit agreement in the strict sense of the term.

The guarantors should be included in the scope of the Directive.

Question 4.2:

In this event:

4.2.1. Should this be limited to coverage exclusively of guarantors in the context of a credit agreement falling within the terms of the Directive?

4.2.2. Should coverage be also provided for commitments relating to a credit agreement *not* falling within the terms of the Directive but which are made by natural persons acting for non-professional purposes?

The person providing a personal security or a real security should be informed of the existence of credit agreements and default by the main debtors.

Guarantee contracts should include a minimum of data, indicating in particular the “amount guaranteed”, which can relate only to the sum in principal of the credit agreement and the arrears interest which may be due by the consumer, excluding any other indemnity or penalty. It would be abnormal for the guarantor to pay non-performance charges incurred by the consumer.

Furthermore, a creditor ought not to be allowed to call upon the guarantors before he has confirmation of default by the main debtor.

5. MORE EQUITABLE CONSUMER PROTECTION

5.1. Sales method

The national regulations banning door-to-door selling and other sales techniques, and cooling-off periods, are very varied³¹.

Several Member States prohibit certain forms of unsolicited approaches and even provide for a total ban³² on canvassing the consumer for credit agreements at home and at work.

Question 5.1:

5.1.1 As regards the ban on canvassing:

5.1.1.a) Should a ban of this kind be harmonised?

5.1.1.b) What level of harmonisation should be sought?

5.1.2 With regard to the cooling-off period in other cases, should provision be made for a harmonised and generalised seven-day withdrawal period?

5.2. Maximum rates and usurious rates

Several Member States have introduced a system of maximum rates and/or usurious rates³³. The report on the implementation of the Directive revealed major differences of approach across the Member States and expressed the Commission's hope that the debate on usury could be addressed at the Community level³⁴.

Question 5.2:

The Commission would like to receive points of view on the pros and cons of adopting measures to introduce a system of minimum rates and/or usurious rates at the European level.

5.3. The supply of credit

It is up to the consumer — and to the consumer alone — to use his credit as he/she thinks fit and in conditions which are completely clear. Any restrictions by the lender to the making available of or to the right of drawing on the sums made available should be justified by the lender. These restrictions should be transparent and should not be a means of surreptitiously remunerating the lender or the intermediary or pressurising the consumer to enter into an agreement without his being aware of all the conditions of cost or repayment.

Such restrictions should, moreover, be examined from the point of view of unfair terms, e.g. a clause obliging the consumer (as a condition for drawing on credit amounts) to pawn all or part of the capital borrowed or to use all or part of it to establish a deposit or to purchase capital goods or other financial instruments.

Question 5.3:

In view of this, would it not be preferable:

5.3.1 for the lender not to be able to make credit available to the consumer until the latter has signed the credit agreement?

5.3.2 for the consumer not to be obliged to start repayment until the credit is placed at his disposal? Should not the lending interest rate begin to be chargeable only as from when the credit is made available?

5.3.3 for the lender to continue to be responsible for the sums (or the goods) he has handed over to the credit intermediary in performance of a credit agreement, until they are all transferred or handed to the consumer or to a third party designated by the consumer?

5.3.4 for sums (goods/services) not to be handed to a third party other than with the express agreement of the consumer?

5.4. Early repayment

There is a tendency³⁵ is to seek to strengthen and extend the right of early repayment, particularly with regard to real estate credit.

Question 5.4:

Is it still justified to claim from the consumer an indemnity or some sort of financial compensation with regard to the credit covered by the Directive, given the possibility of replacing capital on the international market?

5.5. Joint and several liability of the lender and the supplier

A substantial number of disputes arise between consumers and the suppliers of goods and services funded under a credit agreement. Drawing on the rules of common law, the Commission, in its initial proposal for a Directive 87/102, considered giving the consumer the option of taking action directly against the lender without being obliged to first institute proceedings against the supplier of the goods or services. This approach is based on the notion that the signing of a contract of supply of goods or services is conditioned by the existence of a credit agreement. This generates a certain form of joint and several liability between the supplier of goods and services and the lender, and holds a number of legal implications for the latter.

The formula ultimately adopted in Article 11 (subsidiary liability) is the result of a compromise. It stipulates that in certain circumstances the consumer can request payment from the lender if the complaint against the supplier is justified and the latter does not indemnify the consumer. The transposal of this article has nevertheless given rise to a certain volume of ineffective legislation³⁶ in some Member States. In others, particularly France, Germany and the United Kingdom, the legislation has gone well beyond the principle set out in Article 11³⁷.

The examination of these models justifies the request to streamline the conditions set out in Article 11(2). Use of the word “exclusively” could thus be dropped. Moreover, if it were deemed to be appropriate to harmonise, it would then be necessary to opt for a clearly defined system, and not an incomplete or hybrid system which would not work in practice. If there is no case for excluding other proposals or arrangements, it would

nonetheless be necessary to opt for clarity and optimum protection for all credit agreements.

Question 5.5:

The following questions need to be addressed:

- With regard to the degree of solidarity:

5.5.1 Is there a case for maintaining Article 11 and simply dropping the notion of “exclusivity”?

5.5.2 Should an additional step be taken and a principle of solidarity introduced as soon as a consumer uses a means of payment the effect of which entails drawing directly or indirectly on his credit line?

5.5.3 If so, is there a case for introducing a mechanism which would be based on one of the existing national systems, and if so, which?

5.5.4 If a mechanism of this kind is selected, should there in any event be a pre-existing agreement between the supplier of goods and services and the lender?

5.5.5 If so, is it admissible for the consumer not to have to prove the existence of this pre-existing agreement when the supplier is also a credit intermediary and has been involved in the conclusion of the credit agreement?

5.5.6 If principles of joint and several liability between the lender and the supplier are selected and if there are pre-existing agreements between them, should provision be made, as is the case in the UK legal system, for limits on the amounts covered by this mechanism or not?

- As regards the order of action:

5.5.7 Is there a case for giving the consumer the right to take action directly against the lender when it is clear that the latter benefits from commercial advantages by operating with certain suppliers and has — commercial — means of action?

5.5.8 Would it be appropriate or not in this respect for the consumer to first approach the supplier?

6. IMPROVING THE PROCESSING OF PAYMENT DEFAULT

6.1. Forestalling the risks of default: insurance

It is in the interests of the lender and the consumer alike to head off the risk of payment default. The insurance described in Article 1a, 2.v of Directive 87/102/EEC is the most appropriate instrument in this respect.

The current situation is nevertheless not satisfactory. There are three main reasons for this:

- it is extremely difficult to distinguish between the situations where insurance is optional and those in which it is compulsory;
- when compulsory, the cost of insurance should be incorporated in the APR. However, when this insurance is optional this is not done. This situation generates artificial distortions to competition when, despite its optional nature, the agreement of the lender is tacitly subordinated to the taking out of insurance by the consumer;
- when the insurance is compulsory or unavoidable, the consumer does not often have a real choice of insurer. This shortcoming with regard to choice can have significant implications with regard to the overall cost of the credit to the consumer and can provide additional profit to the lenders.

Question 6.1:

Of the four options identified, which would seem to be the most suitable:

6.1.1 Increase the consumer's freedom of choice by giving him the right to organise his own insurance arrangements, including by means of insurance already taken out, and guaranteeing in parallel maximum transparency of premiums and commissions to be paid if he opts for an offer made by the lender, the credit intermediary, or the insuring third party designated by them?

6.1.2 Supplement Article 1a of Directive 87/102 by provisions for the compulsory incorporation in the cost of insurance in the APR unless the insurance offered is not an implicit or explicit condition of the granting of credit, and provided that this has been clearly explained in writing to the consumer and that the consumer confirms explicitly that he/she wishes nonetheless to take out insurance when the amount of the premium has been indicated to him/her? Total transparency with regard to premiums and commissions should also be guaranteed.

6.1.3 Accept a system which would make it possible to distinguish between an APR with insurance and an APR without insurance, and see that it is applied throughout the European Union?

6.1.4 Incorporate into the Directive an obligation for the lender to take out compulsory and comprehensive insurance for his credit agreement portfolio against the risk of non-repayment stemming from the cases described in Article 1a, 2.v)³⁸. This could offer many advantages: each consumer would be insured against certain “events of life”, the lender’s risk would be lesser, the cost would be smaller as the insurance contract would be

negotiated by the lender and the risk distributed across the portfolio, competition would still enter into play, etc.?

The feasibility of this fourth option has been closely examined by the Commission. Summing up:

- compulsory comprehensive insurance of the credit agreement portfolio is technically possible;
- it is nevertheless important to enable the insurer to retain the possibility of analysing before endorsing the insurance contract the lender's portfolio, and any new agreement signed after taking out an insurance, and to allow him to refuse risks he considers to have been taken by the lender outside the rules of caution and good business management, or risks in respect of which the insurer has information concerning the situation relating to the consumer and the likelihood that the latter will be unable to fulfil his obligations, in full respect of the rules which exist on the protection of privacy;
- having the arrangements envisaged concerning the positive or negative information centres would reduce the risks enumerated above;
- the insurance obligation would make it possible to create a genuine market for this type of insurance, would avoid bilateral agreements and would thus contribute to reducing the cost of such insurance.

6.2. Non-performance of contracts

The problems stemming from non-performance concern both credit agreements and security contracts, and involve late payments, tacit or unauthorised overdrafts and also total non-performance.

Generally speaking, all charges and the rates applicable in the event of non-fulfilment of contractual obligations should feature in the credit agreement. Member States should also be urged to ensure that there is a balance between the rights and obligations of the two parties concerned.

Tacit or unauthorised overdrafts, a factor of excessive debt and a real danger for lender and consumer alike, should as a general rule be filtered out. Exceptions or a period of tolerance could be considered. In this event, the rate applicable to the excess should be calculated in a harmonised way and its communication to the consumer should always be guaranteed. At the close of this period, any persistent tacit excess, taking due account of a new appreciation of the client risk, should be regularised by means of a new credit agreement or, if necessary, it should be possible to terminate the contract.

A number of arrangements can be considered:

- 1) As regards the procedures involved:

- The principle of a prior formal notice (which presupposes that there can be no automatic termination), leaving the consumer a reasonable period to make up the shortfall or request rescheduling of his debt, should be adopted.
- Both the consumer and the guarantor should be able to have promptly at their first request a free and detailed breakdown.
- The creditor should first approach the consumer, formally request payment and confirm that there is default before turning to the guarantors.
- Certain debt collection actions should be considered as illegal³⁹.
- A better control by the courts should be introduced in the context of repossession of goods⁴⁰.

Question 6.2.1:

The Commission urges you to submit your comments on these ideas.

2) With regard to the charges which can be claimed in the event of default of payment.

- In certain Member States only interest on overdue payments can be applied, excluding all other charges (except legal charges).

However, the rules on non-performance and the methods of debt collection vary from one country to another. In Belgium, for instance, the majority of cases of non-performance are resolved by applying the procedure of direct transfer of remuneration⁴¹ by registered letter to the employer, pension fund, etc., while in France this procedure would need court action. The cost structure is therefore different.

Question 6.2.2:

It is therefore proposed not to introduce new rules for the time being with regard to the methods of compensation. Are there any counter-arguments?

6.3. Overindebtedness

A directive concerning harmonisation of national legislations on credit agreements is not the appropriate context for a general solution to the problem of overindebtedness, as this problem is a multifaceted one. However, insofar as there is no doubt whatever that consumer credit, particularly in its modern forms, is increasingly a major contributory factor to overindebtedness, preventive steps are proposed in the current draft.

In particular, prevention can be improved through arrangements such as those envisaged by making the partners involved more responsible; by making provision, for instance, for a framework for databases; introducing if necessary a system of portfolio insurance covering certain “events of life”, etc.

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¹ Council Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit.

² Council Directive 90/88/EEC of 22 February 1990 amending Directive 87/102/EEC for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit, OJ No L 061, 10/03/1990, p. 0014 - 0018, itself amended by Directive 98/7/EC European Parliament and of the Council of 16 February 1998, OJ No L 101, 01/04/1998, p. 0017 - 0023.

³ European Commission, Report on the operation of Directive 87/102, COM (95) 117 final.

⁴ European Commission, Summary report of reactions and comments, COM (97) 465 final.

⁵ Communication from the Commission — Financial services: enhancing consumer confidence — Follow-up to the Green Paper on “Financial services: meeting consumers’ expectations”, COM (97) 309 final.

⁶ LEA, M.J., WELTER, R., DÜBEL, A., “Study on mortgage credit in the European Economic Area. Structure of the sector and application of the rules in the Directives 87/102 and 90/88. Final report on tender n° XXIV/96/U6/21 SECKELMANN, R., “Methods of calculation, in the European Economic Area, of the annual percentage rate of charge, Final report 31 October 1995 contract No AO 2600/94/00101; REIFNER, U., ‘Harmonisation of cost elements of the annual percentage rate of charge, APR’, Hamburg 1998, Project No AO-2600/97/000169. DOMONT-NAERT, F., et LACOSTE, A.-C., “Etude sur le problème de l’usure dans certains états membres de l’espace économique européen, Louvain-la-Neuve 1997, Contrat No AO-2600/96/000260 ; DOMONT-NAERT, F., et DEJEMEPPE, P., “Etude sur le rôle et les activités des intermédiaires de crédit aux consommateurs”, contrat No AO-2600/95/000254, 1996 ; BALATE, E., et DEJEMEPPE, P., “Conséquences de l’inexécution des contrats de crédit à la consommation.” Etude AO-2600/95/000270 European Commission, rapport final.

⁷ See the recitals to Directive 87/102/EEC, OJ No L 42, 12.2.87, pp. 48 et seq.

⁸ As amended by Directive 90/88/EEC.

⁹ The Directive was proposed at the end of the 1970s at a time when credit arrangements other than hire purchase were only beginning to appear, and was transposed at the end of the 1980s by which time personal credit/loans had become the predominant formula. This is why the Commission had already proposed in its report on the implementation of the Directive to amend it so as to adapt it to trends in the financial techniques used (see Report on the operation of Directive 87/102, COM (95) 117 final, p. 3, No 15). Furthermore, the Commission had from the outset wanted the Directive to apply to all types of consumer credit. Exceptions obviously had to be provided for, but the Commission was determined to keep them to a minimum. This approach was not however shared by Council which, still deciding by unanimity at that time, had set out a long list of exceptions in Article 2 although the Member States did not make systematic use of them.

¹⁰ See Report on the operation of Directive 87/102, COM (95) 117 final, p. 104, No 384 et seq. and the Summary report of reactions and comments, COM (97) 465 final, p. 20, No 87.

¹¹ This definition corresponds *mutatis mutandis* to the definition which features in the other consumer protection Directives.

¹² German law relates to all natural persons unless the agreement stipulates that the credit is intended for the pursuit of an already existing professional activity. Credit for funding the starting up of a professional activity therefore remains subject to German law. The United Kingdom defines the consumer or rather the debtor as being the person (“the individual”) who has received credit under a consumer credit agreement, including the person whose rights and obligations have been transferred by transfer or entitlement. This person may be a partnership or any other association of persons not entirely made up of legal persons.

¹³ Examples: a lawyer using credit to purchase a car for simultaneously professional and personal use; credit used simultaneously to refinance existing consumer credits and reimbursement of a commercial debt.

¹⁴ Any specific features of a credit contract should if necessary be taken into account by including appropriate provisions.

¹⁵ European agreement on a voluntary code of conduct on pre-contract information relating to housing loans (March 5th, 2001).

¹⁶ E.g. the “Grundschuld” in Germany: see B. VORMS, “L’expression du taux effectif global en matière de crédit hypothécaire”, (study conducted for the European Commission, No B5 – 1030/92/013150), 1993, page 37; a mortgage now exists in Belgium for every claim, etc.

¹⁷ Some information on certain countries to illustrate this issue:

- Germany has no ceiling except for credit granted to a private individual to finance the starting up of a professional activity (DM 100 000) (i.e. EUR 52 000), amended to EUR 50 000). The threshold of DM 400 has been replaced by EUR 200 (§3(1) 1 and 2 Verbraucherkreditgesetz).
- Austrian law has no ceiling and is applied to credit agreements above EUR 20 000.
- Belgium has adopted this exclusion only partially with regard to certain formal provisions, and, as for the ceiling, only in combination with the exemption referred to in paragraph 4.
- Denmark uses neither ceiling nor threshold, except in relation to the chapter on the information obligation for the lender for which the threshold is DKK 1 500 (EUR 196) (§3, paragraph 3, 1, Lov om kreditaftaler).
- In Finland, certain national provisions do not apply to credit under EUR 200 and special rules apply to the early repayment of sums above EUR 20 000. However, there is no real ceiling.
- France has no threshold and excludes credit agreements for a credit equivalent to or higher than FF 140 000 (EUR 21 342.86) but with the exception of provisions with regard to publicity on free or promotional credit (art. L.311-3, al. 1er, 2°, et al. 2, Code de la consommation ; décret n°88-293, article D.311-1). These amounts have not been reviewed since 1988. In order to appreciate the amount of a credit line granted for an unlimited period as an overdraft, the amount of the credit which is to be noted is that of the overdraft reached after the first three months of use of the facility offered to the client (Cour d’Appel de Toulouse, 3ème ch., 2 avril 1996, n° 96-498, Bull. Inf. Cass. 01/10/1996: the law covers only the amount of the sum lent so no account is taken of the total cost of the credit).

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- Ireland uses neither ceiling nor threshold, but excludes loans against security granted by an approved “pawnbroker” (section 3(2) c of the Consumer Credit Act)¹⁷.
 - Luxembourg set its threshold and ceiling on the basis of the Belgian law of 19 July 1957 (which was repealed in 1991): LUF 7 500 (EUR 185.92) and LUF 1 000 000 (EUR 24 789.35) Article 3, 1, f) of the law on consumer credit).
 - The Netherlands do not have a threshold for small sums. Article 3(3) of “consumentenkrediet” stipulates a threshold for sums in excess of EUR 40 840 (NLG 90 000).
 - In 1998 the United Kingdom set a ceiling of EUR 43 381 (GBP 25 000). However, this ceiling does not apply to advertisements or special offers, approval of broker or usury credit. An increase in the amount of credit (ceiling) initially agreed with a second credit does not prevent the law continuing to apply, even if the GBP 25 000 limit is reached, except in the event of a current account advance. The variability of the rate cannot trigger an automatic change to the field of application.

¹⁸ Excluding costs arising from non-performance of the credit agreement.

¹⁹ Reference should be made to the comparison table published in the Report on the operation of Directive 90/88/EEC, COM (96) 79 final of 12.04.96, paragraph 97, p 24, and to the situation of the USA which has similar legislation and goes further as regards the condition of exclusion than the Directive (USA code, Title 15, Title 15, Section 1605 (b)).

²⁰ As regards insurance, see point 6.1 below.

²¹ Accordingly, if a difference of 0.1% to 0.2% is not significant for small credits (particularly when compared with the rates of 200 to 300% (and over) applied by the money-lenders in the United Kingdom and Ireland) the same is not true of high amounts of credit repayable in the short term where the difference expressed in monthly amount can be several euro.

²² Satisfactory transparency is thus obtained while avoiding a situation in which the calculation of periodical interest is carried out in countless ways using different rules pro rata temporis which have but a vague relationship with the linear nature of time. A proportional periodical rate does not correspond to the real cost but generates charges higher than the consumer has accepted.

²³ See Report on the operation of Directive 90/88/ – COM (96) 79 final of 12.04.96, p. 7, No 26.

²⁴ See Report on the operation of Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit – COM (95) 117 final of 11.05.95, paragraph 27 and 219. Summary record of reactions and comments, COM (97) 465 final of 24.09.97, No II.9.

²⁵ Compare with Commission Recommendation 92/48/EEC of 18 December 1991 on insurance intermediaries.

²⁶ As provided for inter alia in Belgian, French, Luxembourg and Dutch legislation.

²⁷ German legislation stipulates that the “credit mediation” agreement must be drawn up in writing and must mention the commission required by the credit intermediary from the consumer in the form of a percentage of the amount of credit, failing which the contract will not be valid. The agreement must also, where applicable, mention the commission granted by the lender (section 15 VerbrKrG). The commission is payable only if the credit has been granted and the consumer can no longer invoke the right of withdrawal. If the credit agreement is intended for the advanced repayment of another credit, the commission will be payable only if the APR (excluding the amount of the commission) of the new credit is not higher than that of the credit to be repaid and the intermediary was aware of the purpose (§16 VerbrKrG). If the credit agreement is used to fund a service, no additional commission can be charged to the consumer except for

the reimbursement of advances (necessary outgoings paid by the intermediary — *“daß dem Kreditvermittler entstandene, erforderliche Auslagen zu erstatten sind”* — (§17 VerbrKrG).

²⁸ E.g. Belgium and the Netherlands.

²⁹ Typical examples are “open end lease” agreements and “balloon” agreements.

³⁰ See the conclusions of the Advocate General Mr Philippe LEGER of 28 October 1999 and the judgment of the Court (fifth chamber) of 23 March 2000 in the case C-208/98 Berliner Kindl Brauerei AG against Andreas Siepert: a contract of guarantee does not fall within the scope of Directive 87/102/EEC.

³¹ The current situation can be briefly summarised as follows:

- Germany provides for a seven-day cooling-off period (“Widerruf”), except for the opening of credit involving only the quarterly payment of interest with no other charges and which are payable any time with no additional charges. This period starts as from the time the consumer is given comprehensible and clear information on the existence of this option (§ 7 VerbrKrG.).
- Belgium gives the consumer the right to “renounce” within seven working days of the day the agreement is signed, when the agreement is concluded in the presence of two parties external to the company of the lender or the credit intermediary and a right to “renounce” within seven working days of the date on which the agreement is signed when the agreement is signed on the day as of which a credit offer is validly handed to the consumer, with the exception of hire purchase or leasing arrangements (Article 18 of the Law on consumer credit).
- In France the borrower may renounce his commitment within seven days of accepting an offer. A detachable form is annexed to the initial offer in order to allow this option of withdrawal to be exercised.
- Ireland provides for a right of withdrawal of ten calendar days starting on the date the credit agreement is received by the consumer. The latter may renounce this right by signing a separate declaration containing notice that by so doing he/she renounces his/her rights. The right of withdrawal is not valid for a housing loan, credit granted via a credit card or an overdraft offered by a credit institution (section 50 of the Consumer Credit Act).
- Luxembourg gives the consumer a right to withdraw from the agreement contract but only for credit agreements granted by a supplier. This right of withdrawal is fully authorised and must be done in writing within two days.
- The United Kingdom grants a cooling-off period to credit agreements which are “cancellable agreements”) but not to credit agreements which are secured by an “interest in land”, which are used for the purchase of property or bridging credits, and credit agreements which are signed by the consumer on the premises, including temporary premises, of the company, lender or “negotiator”: broker, seller, etc. (see Section 67 of the Consumer Credit Act). The existence, running and operational conditions of the cooling-off period must be communicated to the consumer either with the copy of the agreement, or by notification within seven days after signing of the credit agreement (compare Section 62-64 of the Consumer Credit Act). Exceptions are listed in the “Statutory Instruments”. The lender must abide by a series of formalities. The consumer must in principle exercise his right within five days of the day he received the copy of the credit agreement or the day of notification of the existence of his right. This time limit can be extended to 14 days following the day on which the agreement was signed in the event exceptions to the prior notification have been agreed (Section 68 of the Consumer Credit Act).

³² And not only a period of reflection as stipulated in Article 4 of Council Directive 85/577/EEC of 20 December 1985 on protection of the consumer in respect of contracts negotiated away from business premises.

³³ In particular France, the Netherlands, Italy, Belgium and, in part, Portugal and Spain.

³⁴ See Report on the operation of Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit – COM (95) 117 final of 11.05.95, paragraphs 273-297. Summary record of reactions and comments, COM (97) 465 final of 24.09.97, p. 17, No II.12.

³⁵ Accordingly, in France, for instance, the revolving indemnity is no longer due for all consumer credits and, for mortgage credits, is no longer due if the repayment of the latter is explained by the sale of the property following a change of location of professional activity of the borrower or his/her spouse, by a death or by the forced cessation of their professional activity.

³⁶ See in particular Article 24 of the Belgian Law of 12 June 1991 on consumer credit.

³⁷ Three models are to be found in the Member States which have gone beyond the provision of the Directive:

(1) France has introduced the concept of “**linked credit**”. This concept is to provide for the situation in which the conclusion of the sale is subordinated to the party concerned obtaining a loan and vice versa. This is why under French law there is an obligation on the one hand for the professional, seller of goods or provider of services, to specify in the contract of sale or supply that the payment of the price will be made by means of a credit (Article L.311-23) even if the purchaser refuses the loan proposed to him by the seller and uses a credit from a body of his/her choice, and, on the other, for the credit organisation to mention the commodity or service financed by the credit (Article L.311-20). The interdependence between these two agreements is fixed at two key moments (a) when they are signed and (b) when they are performed.

(2) Germany has introduced the notion of “**wirtschaftliche Einheit**” (economic unit). A purchase agreement is a transaction linked to the credit agreement when the credit is used to finance the purchasing price and when the two agreements have to be considered as an economic unit. It may be assumed that there is an economic unit when the lender involves the seller in preparing or concluding a credit agreement (§9(1) VerbrKrG). The purchase agreement can go ahead only if the consumer has not used the right to withdraw from his credit agreement. The contractual clause on withdrawal must refer to this right. Withdrawal remains valid even if the sum lent has not yet been paid back. The consumer can refuse repayment if he can invoke litigation which releases him from his obligations in relation to the seller.

(3) The United Kingdom has maintained its formula of “**joint and several liability**”. Section 75 of the British Consumer Credit Act (BCA) governs “*the liability of the creditor for breaches by the supplier under a debtor-creditor-supplier agreement*”. If the lender is closely associated commercially with the supplier of the goods or services in question, the damage, in the event the consumer were to receive defective goods or services, or a part of the goods or services ordered, or received nothing at all, must be borne by the lender and the supplier. The consumer must have the right to take action against one or the other or both in order to recover the amount of the damage suffered. This article does not apply to all credit agreements but only to those mentioned in Article 12b and c of the BCA, i.e. “*credit agreements which are made under pre-existing arrangements, or in contemplation of future arrangements, between the creditor and the supplier*”. The notion of “exclusivity” and the requirement for prior proceedings against the supplier have not been adopted.

³⁸ There is a need to examine whether the case of “unemployment” can be covered and to accurately determine the events involved.

³⁹ See in particular Article 46 of the Irish Consumer Credit Act and Article 39 of the Belgian law.

⁴⁰ See Report on the operation of Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit – COM (95) 117 final of 11.05.95, paragraph 184 to 188. Summary record of reactions and comments, COM (97) 465 final of 24.09.97, No II.5.

⁴¹ Based on a contractual agreement when the credit agreement is signed.