

Credit agreements relating to residential property

Proposal for a Directive

BEUC position

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Summary

BEUC welcomes the long-awaited legislative proposal on credit agreements relating to residential property which aims at protecting all retail borrowers across Europe. Our main requests for amendments are as follows:

- combine a high level of consumer protection with a minimum harmonisation approach;
- complete the Commission proposals as regards the conduct of business obligations and minimum competence requirements by additional rules to ensure the implementation of those proposals;
- enable competent authorities of the host country to play an important role in supervision of creditors and intermediaries: in this perspective we prefer a 'European driving license' rather than a 'European passport';
- adopt additional provisions regulating some aspects of future developments of the credit contract, including prolongation issues;
- ensure that all the identified problems in the application of the Consumer Credit Directive regarding advertising and pre-contractual information are properly taken into account;
- Adapt the APRC definition to include all tied ancillary services.
- address the issue of variable interest rates: adopt provisions capping the rise of interest rates and protecting consumers from being overextended by rising interest rates as well as means to stop or freeze rates in case of peculiar market developments that would otherwise cause masses of consumers to default;
- make lenders and intermediaries responsible for asking the right questions, requesting borrowers to provide the right supporting documents and collecting the relevant data;
- restrict the cross-border data exchange to negative credit data only;
- remove the provisions concerning sanctions against consumers;
- add provisions aiming at the development of truly independent advice;
- redraft the Commission proposal to offer consumers a real right of early repayment.

Borrowing money to build or buy a home is the single most important financial decision in most people's lives, one which engages them for 20, 30 years or longer. Borrowers cannot afford to be sold a bad deal. One of the lessons of the financial crisis has been on inadequate protection of borrowers in many EU countries: unsuitable loans, misinformation, aggressive marketing, lack of information on risks linked to using foreign currency and superficial assessment of people's financial means have made many loans increasingly unaffordable, raised defaults of payments and seen an increase in foreclosures.

The European Commission's impact assessment accompanying the proposal for a Directive on credit agreements relating to residential property provides very strong arguments in favour of an EU action.¹ The document states that, although not to the same degree as in the US, facts of irresponsible lending exist in different EU Member States. Furthermore, some risky products such as self-certified mortgages disappeared from the market during the crisis showing the uselessness of some financial innovations which led to highly complex and risky mortgage products. On the other hand, even if high loan-to-value mortgages substantially diminished when the crisis began, they have already made their reappearance showing the failures of the market and the weaknesses of regulation.²

How can we ensure that socially harmful risk taking driven by lenders' wish to make a profit is not resumed once the crisis enters the annals of history? We believe this can only be achieved if the duties and responsibilities of every lender and credit intermediary operating on the home loans market are properly defined and enforced. BEUC position in this respect was already expressed in our response to the public consultation run by the Commission in 2009: all products, all sellers, all marketing channels must be taken into consideration and comply with the same rules in order to avoid market distortions and guarantee a level playing field for all market participants.³

BEUC welcomes the long-awaited legislative proposal on credit agreements relating to residential property as it pursues two main goals which are particularly important for European consumers:

- First, **protect all borrowers across Europe** (responsible lending perspective). From a consumer perspective the priority is to strike the right balance between ensuring a high level of protection for all EU consumers and preserving already existing national consumer-friendly legislation. Furthermore, in some Member States home loans legislation is in the process of being adopted or revised. Those Member States should be able to adopt higher consumer protection standards and should not, for instance, have the European Standardised Information Sheet (ESIS) forced upon them where adequate information sheets are already in place. This is the reason why **this Directive should at the same time provide a high level of consumer protection and be based on a minimum harmonisation approach**. The approach adopted by the Commission varying from principle-based standards to high-level harmonisation provisions and maximum harmonisation depending on different areas of the proposal should be amended accordingly.

¹ Accompanying document to the proposal for a Directive of the European Parliament and of the Council on credit agreements relating to residential property:

http://ec.europa.eu/internal_market/finservices-retail/credit/mortgage_en.htm

² For example, compliance rate with the code of conduct on pre-contractual information for home loans (ESIS) adopted in 2001 is not satisfactory.

³ "Responsible lending and borrowing in the EU", BEUC response to public consultation, September 2009: <http://www.beuc.org/Content/Default.asp?PageID=2143>

- Second, create a level playing field between bank and non-bank mortgage providers and intermediaries (competition and single market perspective) by applying the same rules to all parties engaging in the business of providing home loans.

Some changes and further provisions are needed to amend the Commission's proposal to meet the set goal i.e. to better protect consumers and the market:

- **Conduct of business obligations and minimum competence requirements:** BEUC welcomes the provisions of articles 5 and 6 to focus on the interest of the consumer with respect to the conduct of business. This is a valid approach which however needs to be completed by additional rules to ensure its implementation. BEUC members have further identified unfair and potentially dangerous commercial practices concerning products and sales procedures including tying with ancillary services as well as complex products that need to be adequately dealt with.
- We welcome a **strict approach of supervision** but we would favour a **'European driving license'** rather than a 'European Passport'. Competent authorities of the host country will need to supervise where someone is doing business and in case of relevant failure have the ability to revoke the provider's general access to the Internal Market. In the same spirit, national authorities can revoke someone's driving license which will prevent him from driving in any other country. This is essential to prevent further failure in up to 26 other Member State markets.
- Although home loans are not only the economically most important contracts a consumer will conclude but also among the longest to run, the provisions of the proposal for Directive almost exclusively deal with the conclusion of the contract. This is the reason why it is important to adopt additional provisions regulating some aspects of **future developments of the contract**, including prolongation issues.
- Most of the information duties concerning **advertising and pre-contractual information** are similar to the Consumer Credit Directive. It is essential to ensure that all the problems which have been identified when the Consumer Credit Directive was implemented are properly taken into account. E.g.: provisions on compulsory information in advertisements should be based on a representative example (to be defined at national level) and never be mentioned in small print while the overall message of the advertisement is in bigger print.

It is also crucial to ensure that consumers get the pre-contractual information immediately and well before they make a decision as they need it to be able to shop around within a reasonable period of time.

In so far as efficient information sheets have already been implemented in some Member States, they should be allowed to keep them or further develop enhanced versions of ESIS. At the moment, home loans markets differ extensively, this is the reason why different approaches to information sheets should be allowed to exist as long as they serve the interest and find approval of consumers.

The **Annual Percentage Rate of Charge definition**, as stated in the Consumer Credit Directive (CCD), already applies in some Member States for home loans. However this definition is not always fully adapted to some mortgage credits, notably to complex products. E.g. all tied ancillary services need to be included in the APRC. There is a need to adapt the APRC definition included in the CCD to mortgage credits.

- **Variable Interest Rates** have sometimes proven to be a threat not only for consumers but also for the market itself. Measures protecting consumers from being overextended by rising interest rates as well as means to stop or freeze rates in case of peculiar market developments that would otherwise cause masses of consumers to default are missing. Capping the rise of interest rates - at least by compulsory contractual provisions - is a matter of fairness both for consumers and lenders: while floor caps are usually set in such way that lenders refuse to serve the contract if rates are too low, in general there are no ceilings (or no adequate ceilings) set in order to also protect borrowers when interest rates rise too high. Creditworthiness assessment should check that top level interest rates enabled by the provisions are still servable by the individual consumer. A similar risk arises with foreign currency home loans.
- While the Draft Directive draws a line between creditworthiness assessment and proper information and adequate explanation, one should really focus on preventing the conclusion of unsuitable contracts that are likely or bound to fail. We consider it to be more important to ensure that the product is not inadequate to meet the needs of the consumer rather than to assess solely the creditworthiness of the consumer. A consumer should not be left over-indebted because contractual concepts did not work out as regards repayment instruments or because property assessment was not duly done and communicated e.g. to warn the consumer about a significant difference of financed price and backing property. We ask that if the evaluation of the value of the property was not made properly, a court may declare that the debt will be fully annulled after repossession.

It is in consumers' own interest to prevent mistakes and defaults. However few consumers are experts in home loans, thus it is the duty of lenders and intermediaries to ask the right questions, request borrowers to provide the right supporting documents and collect the relevant data. Relevant data needs to be clearly restricted to the necessary data to proceed the loan and the assessment.

Furthermore **cross-border data exchange needs to be restricted to negative credit data only** (information on an individual's default record) as this is the only data present in all Member States and that cannot be misinterpreted; use of positive data (information on an individual's credit exposure) will always depend on further assumptions that may turn up very differing results from one Member State to another. Though Member States share common data protection standards, there is at this stage no rule on how consumers can deal with the exchange of faulty data. This is the reason why additional provisions should be adopted in order to apply the decisions of data protection authorities on data exchanged with other countries as well as to apply these provisions to those countries.

- BEUC and its members strictly reject the proposal of further **sanctions against consumers**. In case consumers act fraudulently there are already sufficient provisions, including criminal law in place at national level.

Failure of the contract and loss of one's home, sometimes years after making it as a centre of one's family life, may well be assumed to be already the worst sanction possible to a consumer; there is definitely no need to put further pressure on them by threatening with sanctions.

- **Independent advice** needs to exclude any conflicting interest when counselling a consumer on the adequate product with respect to the whole market. In our opinion, advice provided by lenders or dependent intermediaries always carries the risk of conflict of interest.

BEUC welcomes the provision that advice is a service itself that has to fully serve the interest of the consumer and be independent of the contract that is to be concluded.

- In some Member States, **early repayment** is restricted partly by law, partly by the specific concept of home loans in the market. The option to repay a loan prematurely is essential to safeguard the contractual freedom of consumers during the course of a long-running contract. Some markets developed very high and non-transparent compensation practices. In Germany, despite the highest compensation, a general right to early repayment does not even exist. There is not one single rule that will fit all markets in an adequate way but there is a general need for fair, feasible and transparent practices that prevent locking consumers in a contract while at the same time considering the way of how contracts are refinanced. This is why additional provisions should be adopted stating specific conditions necessary to ensure that early repayment is a right for each borrower but resulting national laws may yet be different as long as transparency is kept and arbitration is banned.

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