

## TABLE OF CONTENTS

- Failure to implement relevant legislation: guarantees on consumer goods and e-commerce directives
- New developments in contract law
- GE receives authorisation from the Commission to acquire Abbeys National consumer business
- New Forum Group on Mortgage credit
- Consumer credit: the case of language schools in Spain
- Regulation of financial privacy: United States versus Europe: New ECRI study.
- Timetable of the Consumer Credit directive
- EUI Conference programme

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### **Commission warns several member states for failure to implement relevant legislation on guarantee on consumer goods and e-commerce directives**

The Commission has issued a warning to eight member states of the EU for failure to implement EU directives on the sale and guarantee of consumer goods, and to another seven member states for failure to implement the so-called e-commerce directive.

In the first warning, issued to Belgium, Spain, France, Ireland, Luxembourg, the Netherlands, Portugal, and the UK, the European Commission requests these countries, in the form of reasoned opinions, to implement quickly the necessary legislation.

If member states fail to guarantee that the rights of consumers enumerated in the directive are ensured in national legislation, the Commission could start infringement procedures in the European Court of Justice.

The text of the directive was formally approved in May 1999 under the framework of the Third Consumer Policy Action Plan. The provisions should have been transposed by 1 January 2002.

The directive applies to contracts for the sale of new or second-hand consumer goods, and to contracts for the supply of goods to be manufactured or produced that have been concluded between a professional and a consumer.

The two main objectives of the directive are the harmonisation of legal protection and the improvement of protection concerning “commercial guarantees”. It establishes a guarantee period of two years, during which time, if any default of the good involved appears, the consumer is granted four options: price reduction, cancellation of the contract, repair of the good or replacement. If any defects appears during the first six months after the transaction, the good is considered defaulted at the time of delivery and the burden of proof lies with the seller.

When commercial guarantees are voluntarily offered by sellers or manufacturers, the guarantee specifications offered by means of publicity are legally binding, and not only the specifications in the document itself.

The second key directive that several member states have failed to implement in time is the so-called e-commerce directive, whose implementation deadline expired on 17 June 2002.

The European Commission has warned those countries, in the form of reasoned opinions, to quickly enact the pertinent legislation. Countries receiving the warning are Belgium, Greece, France, Ireland, Italy, the Netherlands and Portugal.

The directive was considered essential to the development of on-line financial services. It provided for the so-called “internal market clause” enabling on-line providers to supply services throughout the EU based on the rules of the member state of establishment. However, mirroring the legislation of traditional retail finance, under certain conditions, member states can take measures that restrict the freedom to provide information society services, in particular, for reasons of public policy or the protection of the consumer. Therefore, it was anticipated that problems in cross-border provision would be similar for electronic as for traditional means.

### **New developments in European contract law**

The Commission has adopted an Action Plan setting out a road map that will bring greater coherence in European contract law and will smooth the functioning of the internal market.

So far, *The Rome Convention* determines the law applicable to financial services contracts. But contract law has not been harmonised at European level and has remained in the sphere of international private law, with reference to the laws of each state. This approach involves several inconsistencies such as difficulties in the conclusion, interpretation and application of cross-border contracts and the non-uniform implementation of EC law. The retail financial services industry had for sometime acknowledged the difficulties of cross-border contracts, where it is not possible to know, without local expertise, how contracts will be affected by different clauses.

In July 2001, the Commission presented a Communication to launch a debate on the problems encountered by the single market due to contract law divergences. Four alternatives (see ECRI Newsletter No 2) were proposed, namely:

- Let the market regulate any problems;
- Identify common principles to all national laws, to be applied as guidelines;
- Launch a simplification process aimed at all the existing legislation; or
- Create a new and uniform piece of legislation at EU level.

The responses to the Communication showed that there was no agreement on the most adequate course of action between the parties involved (see ECRI Newsletter No 3). Likewise, the Commission has presented an action plan that represents a long-term strategy composed of a mixture of regulatory and non-regulatory actions. The main measures contemplated are:

- The elaboration of a “common frame of reference” for contract law rules and terminology;
- To promote the use of EU-wide standard terms; and
- To reflect on the adequacy of creating an EU level body to facilitate cross-border contracts across all sectors.

Recent information can be found on:

[http://europa.eu.int/comm/consumers/cons\\_int/safe\\_shop/fair\\_bus\\_pract/cont\\_law/index\\_en.htm](http://europa.eu.int/comm/consumers/cons_int/safe_shop/fair_bus_pract/cont_law/index_en.htm)

### **Commission clears GE acquisition of Abbey National's consumer loan business**

The European Commission has granted regulatory clearance under the Merger Regulation to the proposed acquisition by the US company General Electric of certain businesses of the UK financial company Abbey National Plc. The business that GE is acquiring consists of three legal entities primarily active in the provision of secured and unsecured loans to consumers, in particular point-of-sale credit to customers in the UK. (The deal was notified to the Commission on 26 February 2003, and was examined under a simplified procedure).

See: [http://europa.eu.int/eur-lex/en/dat/2003/c\\_052/c\\_05220030306en00120012.pdf](http://europa.eu.int/eur-lex/en/dat/2003/c_052/c_05220030306en00120012.pdf)

### **Mortgage credit: Commission invites stakeholders to help to open up the EU market**

The European Commission's Forum Group on Mortgage Credit met for the first time on 27th March. The Group includes more than 20 experts from 11 member states. It will advise the Commission on how to make progress towards a genuine European market for home loans, which would make it easier for home buyers to save money by choosing mortgage products from lenders anywhere in the EU. National consumers associations, the credit and insurance sectors and other stakeholders such as European notaries and chartered surveyors are all represented in the Group.

**Timetable of the CCD**

The Commission proposal for a consumer credit Directive was presented on 11 September 2002. Today's credit industry bears little resemblance to the retail credit scene in the 1980s, which inspired the 1987 directive. All parties therefore agreed on the need to update the regulatory framework. The scope of the new directive is extended to all credit and surety agreements including guarantors, with a few exceptions: housing credit for the purchase or transformation of property and credit and advance granted occasionally by an employer to his or her staff. The directive establishes a new framework to redress the sharing of responsibilities between consumers and lenders, including intermediaries.

Timetable of the CCD

11 September 2002	Proposal
21 November 2002	Draft opinion by the ENVI committee
9 January 2003	First meeting of the EU Council experts group
11 February 2003	Document with amendments to the ENVI committee
29 April 2003	Public hearing of the JURI committee
30 April 2003	Vote at the ENVI Committee
19 May 2003	Council Common Position expected

Industry and consumers have expressed disagreement on certain key issues. Eurofinas, the main representative of EU consumer finance companies, together with FEDSA and EUROCOMMERCE have issued a position paper which enumerates the provisions with a likely negative impact on market efficiency, the restriction in the variety of products offered and the creation of imbalances between creditors' and borrowers' obligations and responsibilities.

According to Eurofinas, articles likely to have an impact on market efficiency are Arts. 7 and 8§3 on collection and processing of data from central databases. The industry opposes the requirement to destroy personal data once the credit agreement has been completed. Such records are essential for the construction of a credit scoring system, an essential piece in the operation of today's consumer finance industry.

Point-of-sale finance is a product that deserves special attention. Provisions concerning the right of withdrawal and the return of goods to the lender (Art. 11§1 and 11§3) can lead to the elimination of point-of-sale finance from the market. Other products affected might be current accounts, overdrafts and very small amount credits (Art. 3, 3§2). The industry also claims that the directive misjudges certain

As was the case with previous regulatory initiatives in the field of retail financial services (e.g. directives on marketing of financial services, distance selling of financial services, or the horizontal directive on e-commerce), the parties involved have different views about how to regulate this field for the benefit of consumers and industry and, how to push forward the completion of the internal market.

The text spells out a comprehensive set of provisions that will impact the way the industry and the market function. There are four initial aspects that provoked much controversy, namely, the novel concept of *responsible lending*, the *duty to provide advise* and information requirements prior to granting the credit, and the legislative approach of the directive, in this case *maximum harmonisation*.

products, such as doorstep selling or credit balloon, which in practice have been largely accepted by consumers and have not raised any significant problems.

The industry is also concerned about the confusion that might be created by the inclusion of all the different rates to be presented to the consumer, but without bringing any added-value information. Other industry members largely support these views.

On the other hand, one of the main concerns for consumers, as expressed by the BEUC, is the overall level of protection offered by the directive, which in many cases undermines the existing consumer protection regime in different member states. It therefore urges the Commission to reconsider its objective of maximum harmonisation in this area. BEUC strongly argues in favour of including mortgage and mortgage-backed loans. Consumer associations largely agree with the provisions stipulating the information to be supplied prior to granting credit, the role of credit intermediaries and the introduction of the notion of responsible lending. BEUC regrets however that the burden of proof on lenders is not mandatory in the directive, and points out that still many issues need to be fine-tuned, such as the proposed APRs, the collection and processing of borrower's data or early repayment.

The European Parliament's Consumers Committee published in November its draft opinion, which will be followed by a final opinion after voting the amendments; the vote is foreseen to take place on 30 April 2003. Overall, the opinion of the Committee underlines that the Commission's objective of total harmonisation of the laws and regulations of member states should not diminish the level of consumer protection achieved, and therefore, member states should be granted the possibility of introducing stricter provisions. The Consumers committee has based its draft opinion on the following points:

- The aims of the proposal should be extended to include guaranteeing the consumer a high level of protection.
- The Committee fully agrees with the Commission on the relevance of providing the consumer with the relevant information, but would like the proposal to strengthen this objective.
- Concerning the burden of proof in the assessment of the ability to repay, the Committee would like to see the proposal go further. The Committee proposes a mandatory requirement that the lender should always prove that it has proceeded in a responsible manner to assess the creditworthiness of the borrower prior to grant the credit.

- Early repayment regulation should be left to member states and coverage might be extended.
- Joint and several liability is welcomed but the Committee requests further reach of provisions to all sales by retailers that are not considered credit intermediaries.

In line with the above points, the rapporteur presented 18 amendments to the Committee. Parliamentarians presented a total of 156 amendments for future discussion. The larger number of amendments concerned Articles 2, 3, 5, 6, 7, 8, 9, and 19.

The article referring to exchange of information and the duty to provide advice (Art. 6) received the largest number of amendments, in particular to clarify and specify in detail the type of information provided. The deletion of paragraph 3 on the duty to advise and the presentation of advantages and disadvantages of the product was demanded by four MEPs.

The provisions on the scope of the directive (Art. 3) was also the object of a very large number of amendments, mainly intended to exclude mortgages, mortgage-backed loans, hiring purchase agreements, current accounts, forms of deferred payment and small loans from the directive.

Consultation of central databases and the processing of this type of data are also among the most discussed issues (Art. 8). The conflict between the usefulness and the processing of data with individual privacy protection are the main concerns of MEPs.

Given the divergent views expressed, we foresee a long discussion in the European Parliament before the text reaches a form to which all parties agree.

**Consumer credit in Spain: Consumer credits to finance studies. Have they to be repaid if the school goes bankrupt?**

By Ignacio Pla Vidal, ASNEF (Spanish National Association of Finance Companies) representing the views of ASNEF involving the recent case of *Opening* English language school occurred in Spain.

The main benefit of the “welfare society” is the enhanced prosperity of its members. Such ambitions not only refer to meet basic necessities, but reach further. In order to achieve this goal, the individual will have to employ all resources available, which might be often insufficient. Modern economies however, overcome this scarcity of resources by making available the resources of savers. Financial intermediaries attract money from savings, which is offered to consumers by means of different kinds of credit, and an interest rate is charged to ensure profitability in such a transaction: This operation raises a monetary flow that benefits both parties. Savers obtain a benefit and borrowers can have access to what they deem necessary.

Amongst the different types of credit, consumer credit has expanded notably during the past decades. Consumers have access nowadays to goods and services that were previously only available on conditions of immediate payment. Consumer credit has become a mainstream financing alternative. Washing machines, cameras and family holidays are common examples of financing that show the degree of adoption and satisfaction that consumer credit enjoys in our society.

New social needs have compelled financial intermediaries to offer new financing formulas adapted to the purchase of an increasing variety of goods and services. The use of credit to finance studies is increasingly available to those wishing to expand their education or professional training.

Consumer credit has rarely posed major problems to consumers. Most consumers have on occasion used consumer credit and the contract has been successfully concluded. However, consumer credit has attracted much media attention lately due to the public concerns raised by the bankruptcy of a number of English language schools in Spain, whose students resorted to consumer credit to pay for the courses. The most famous case is *Opening*, the first school that suddenly filed for bankruptcy. Many of the students using consumer finance still have to repay the credit but they no longer attend the lectures.

The English school had already received the payment from the financial institution, on behalf of the student, for the totality of the course to be given. The controversy concerns whether the breach of the contract by the school (by not providing the courses) should automatically provoke the termination of the credit agreement between the lender and the student.

The Spanish consumer credit law (7/1995, 23 March, Art. 14§2) established that “...the ineffectiveness of the contract, whose object is the satisfaction of a consumer need, will equally determine the ineffectiveness of the contract for the purpose of its financing when the conditions in paragraphs a), b) and c) of Art. 15§1 are met, with the consequences foreseen in Art. 9”. Therefore, Spanish legislation is clear on this matter; namely, a financing contract can be declared ineffective if the following sets of conditions are met (Art. 15§1):

- a) That the consumer, for the purpose of the acquisition of the good or service, contracted for consumer credit with a company different from the seller of the good.
- b) That there existed a previous agreement between the lender and the seller, agreed in exclusivity, by which the lender will provide credit to the seller’s customers for the acquisition of the good or service.  

The consumer will have the option of obtain consumer credit from a lender other than the one linked, by the previous agreement, to the seller.
- c) That the goods or services affected by the contract have not been delivered, totally or partially, or they have not been in accordance with the contract.

According to the regulation, the existence of a previous, and in exclusivity, agreement between the seller and the lender is a necessary condition for the ineffectiveness of the contract between the lender and the consumer. Only in this event can the finance contract (lender/student) can be declared ineffective if the teaching contract (school/student) is terminated. Otherwise, the finance contract is effective.

Of the conditions mentioned above only one is not met, that is the exclusive character of the agreement between the school and the lender. The student could finance his/her course via another financial institution different to the offered by the school for the financing of the course.

A different issue is the assignment by the school of the credit agreement to a financial institution. The principle embraced by the legislation for these cases is not to harm the debtor. The transfer does not need the consent of the debtor to be effective, and therefore, according to Spanish legislation, the debtor has the same rights with respect to the financial institution as it would have with respect to the school (Art. 1526 and following of the Spanish civil code in reference to Art. 1203 and 1212).

On the other hand, despite the fact that the deceit has been carried out by the school exclusively, these types of contracts are deemed as misleading. The consumer always knows, as indicated in the credit contract, that he/she is signing a financial agreement, with the corresponding obligations. The lender will have to advance the cash for the payment of the studies and the borrower will assume the repayment of that loan.

Credit institutions are subject to the supervision of the Bank of Spain, which demands disclosure and transparency in their operations with borrowers; the Bank of Spain supervises even advertising.

Therefore, it is assumed that these types of contracts comply with and are drafted according to central bank regulation.

It is advisable to carry out information activities that raise awareness among consumers on the importance and need of reading contracts before signing them. Failure to do so is clearly against their own interests.

Lastly, in the case of *Opening*, public attention seems only concerned with the rights of those students that paid their courses in cash, and have therefore lost all possibility to recover their investment. This means in practice a discrimination between both types of students.

Ultimately, consumer credit is a valid means to facilitate the access to further education for citizens, adding to the human capital base and economic growth of a country.

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### **The Regulation of Financial Privacy: United States versus Europe**

New ECRI Research Report, by Nicola Jentsch, John F. Kennedy Institute, Berlin

The consumer credit market depends on the exchange of information among market participants. Credit bureaus are the primary repositories of this information, and in recent years they have gathered a vast amount of data on consumer spending habits. Until recently, however, there has been little analysis of the far-reaching economic and privacy implications of these firms. There has also been little quantitative analysis of the effects of differing regulatory environments on both these firms and the health of the consumer credit market.

The present study tries to fill that gap by analysing the economic effects of different financial privacy regimes. We contrast the United States with the European Union (reference countries: Germany, the UK and France) to analyse the differences of the privacy regimes in these countries and their effects on consumer credit markets. In the US, less privacy regulations exist and credit bureaus are competing on a nationwide scale. In the EU, on the other hand, data protection and credit reporting schemes still differ

from one country to another, and the provision of cross-border information is underdeveloped. Americans enjoy broad access to credit, but this is correlated with greater indebtedness, whereas in the EU, credit markets are thinner and households are in general less indebted.

One of the major research questions is whether more stringent data protection regulations would inhibit the distribution of credit reports in consumer credit markets. This, in turn, could result in reduced access to consumer credit, less integrated markets and increasing consumer credit risk. We develop a quantitative index, the Financial Privacy Index (FPI), that quantifies data protection regulations. We show that the US grants less data protection than the selected sample of EU member states. Using this index, we identify the effects of data protection on information distribution, access to credit, consumer indebtedness and credit risk.

The international comparison shows that countries with higher data protection are associated with lower information allocation. Growing data protection in individual countries is however correlated with increased information allocation. We show that the more credit reports are sold the higher is the access to credit. This is associated with greater consumer indebtedness and higher household debt-service burden (consumer credit risk). The latter is due to the fact that access is broadened and less creditworthy households enter the market.

These findings have important policy implications for the EU. To increase access to credit and to expand the integration of consumer credit markets, the cross-border distribution of credit reports should be facilitated by a standardisation of European credit reporting systems. The new Consumer Credit Directive provides a chance for such a harmonisation. However, the cross-border exchange has to be transparent to consumers – this is of utmost importance for the trust in consumer credit markets.

Instead of drawing up another directive that explicitly deals with credit information, the European Commission should ensure that the current data protection Directive is equally and quickly transposed in the member countries. A new directive aimed specifically at the exchange of credit information would only increase regulatory insecurity and introduce another round of extended (unequal) transposition efforts by member countries. Moreover, the European Commission should develop a clear and transparent evaluation mechanism for reviewing the transposition of the current data protection Directive.

A positive effect of the increased information exchange at the European level will be the broader access to consumer credit. The negative effect, however, will be increasing consumer indebtedness as well as rising credit risk. Europe needs a unified framework and common definitions of bankruptcy and over-indebtedness of households to effectively monitor these developments.

Note to researchers.

Next European University Institute conference in May

**European University Institute  
Finance & Consumption Conference on  
The Economics of Consumer Credit:  
European Experience and Lessons from the US  
13/14 May 2003**

**Programme**

*Tuesday, May 13th* (Translation in the morning only)

9h30-10h15 *Coffee and Registration*

10h15-10h30 *Welcome Addresses*

10h30-13h00 Session 1: **Introduction to the Facts**, Chair: Giuseppe Bertola

Nicholas S. Souleles [\*] (Wharton School, University of Pennsylvania)  
*Credit-card Borrowing Patterns in the United States*

Jonathan Crook (CRC, University of Edinburgh)  
*The Demand and Supply of Household Credit: Cross-country evidence*

Luigi Guiso (Ente Luigi Einaudi)  
*Credit Access for Italian Consumers*

**Panel Discussion** with Richard Disney [\*], Umberto Filotto, Rosamaria Gelpi, Michael E. Staten, Michelle J. White.

13h00-14h00 *Lunch*

14h00-15h30 Session 2: **Regulating Default**, Chair: Michael Haliassos [\*]

Michael E. Staten (Credit Research Center, Washington D.C. and McDonough School of Business, Georgetown University)  
*Counseling and the Regulation of Financial Services for Retail Customers*

Michelle J. White (University of California, San Diego)  
*Bankruptcy and Consumer Credit in the US*

15h30-15h45 *Coffee*

15h45-18h00 Session 3: **Information Sharing and Credit Bureaus**, Chair: Charles Grant

Tullio Jappelli and Marco Pagano (Università di Salerno)  
*Information Sharing in Credit Markets: A Survey*

Amparo San José Riestra (CEPS) and Nicola Jentzsch (Free University of Berlin)  
*Information Sharing and Its Implications for Consumer Credit Markets: US vs EU*

Robert Hunt (Reserve Board of Philadelphia)  
*The Development and Regulation of Consumer Credit Reporting in America*

### Wednesday, May 14th

9h30-10h00 *Coffee*

10h00-12h45 Session A: **Debt and Equity**

Richard Disney and Sarah Bridges (U. of Nottingham) and Andrew Henley (University of Aberystwyth)  
*Housing Equity changes and Debt-Financed Consumption Spending*

Jeremy Tobacman (Harvard) with David Laibson (Harvard) and Andrea Repetto (University of Chile)  
*Wealth Accumulation, Credit Card Borrowing, and Consumption-Income Comovement*

Michael Haliassos (Cyprus) with Michael Reiter (Pompeu Fabra)  
*Credit Card Debt Puzzles*

12h45-14h00 *Lunch*

14h00-15h30 Session B: **Retail Interest Rate Convergence in the EU**

Natacha Valla, Gabe de Bondt, and Benoit Mojon (ECB)  
*Retail Bank and Market Interest rates: the implications of EMU for Bank Pricing*

Harald Sander (Cologne) and Stefanie Kleimeier (Maastricht)  
*Convergence in Eurozone Retail Banking? What interest rate pass-through tells us about Monetary Policy Transmission, Competition, and Integration*

\* To be confirmed

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