

## **Snapshot of the ECRI seminar on consumer credit and consumer protection**

**7 June 2001**

The objective of this ECRI seminar was to refocus the debate on consumer protection in financial services, with special attention to the foreseen revision of the Consumer credit Directive.

In a debate on what is the appropriate consumer protection regulation required in the European financial area, two notions of the consumer interest need to be taken into account. First, the advantage of cross-border trade to improve the consumer choice and second, the national measures of consumer protection required in view of market failures, such as informational asymmetries.

The seminar treated some of the key issues in the consumer aspect of financial services with the participation of representatives from the European Commission, academics, the views of business and consumers, and the presentation of the USA views on the European Consumer credit area. Some 40 people attended the seminar and participated in the debate.

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### **Session 1**

#### **Jens Ring, European Commission "The revision of the European Consumer Credit Directive"**

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Mr. Ring presented the basis of the next Consultation paper on the revision on the Consumer Credit Directive.

As a consequence of the 1995 report, the Commission has realised that the directive is not any more in line with changes occurred in the market. Several studies in the field of APR, mortgage credit or advertising to children have confirmed it. Recognising the underdevelopment of cross-border activity in the consumer credit area, the Commission will launch a Consultation paper with the following principles:

- Need to adapt the legal framework to new market techniques,
- Re-balancing creditors and consumer rights,
- Achieving a high level of consumer protection.

The paper will follow several guidelines:

- The future directive should cover all the aspect of consumer credit. (No matter the technique or the amount).
- The directive will carefully consider the area of credit intermediaries.
- Introduction of structured information for credit grantors. The directive will study the issues of transparency, quality of information, questions regarding risk assessment and usury among others.
- Introducing more comprehensive information for the consumer and any guarantors.
- Improving the arrangement for payment incidents by professional, introducing standard basic rules and streamlining the way to approach consumes.

The Directive foresees the clarification of several issues, such as credit secured by mortgage, data protection, liability of the seller of good, the consideration of insurance to cover certain risks of payment. It will consider methods based on individual insurance against compulsory portfolio insurance for the credit grantors, and the convenience of insurance taken by the borrower or the lender. Mr. Ring ensured that all the topics will be approached without preconceptions.

The Commission approach moves from minimum harmonisation to maximum and optimal harmonisation in order to achieve a higher level of consumer protection.

### **Mr. Cartwright, University of Nottingham "Optimal consumer protection"**

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Mr. Cartwright presented his paper on optimal consumer protection. The paper considers the economic and social rational for intervening in financial services markets to protect the consumer, paying special attention to the position of vulnerable consumers.

Financial markets regulation can be justified in terms of market failures, such as a limited number of players or barriers of entry, or from social point of view, to protect users of the market.

There are weaknesses to the economic approach, for example, disclosure regimes may bring benefits, but it is difficult to decide at what level they should be set, and may also lead to information overload. In some other examples, regulation can have offset effects, as is the case of supervisory measures to avoid systemic risk, which contravenes the principle of free entry demanded by the perfect market. Intervention may also be more costly than the market failure it is designed to address. Considerations of the role of private law, in particular contractual law, are also important.

It is also possible to examine non-market approaches to regulation. They are based on paternalism and community values and distributive justice. This approach is denounced for treating consumers as a homogeneous entity. Often, such measures have negative distributive effects because they disproportionately benefit only the more affluent and better-educated consumer, reproducing injustice.

In the treatment of consumer protection in financial services Mr. Cartwright proposed to look at issues such as the identification of the vulnerability of consumers in different groups considering information of deficits and asymmetries, the greater susceptibility to loss or pressure that some consumers have and how vulnerability is affected by the extent of choice available, and the risk of discrimination.

Regulation in the field of financial services should provide solutions for all the above issues. He believes that some of them can be delivered by the use of credit ceilings, encouraging the use of new sources of supply, improving the access to justice and further analysis of cost benefit and distribution.

### **Issues raised by participants after the first session**

Concerning Mr. Cartwright presentation Rosa María Gelpi raised the issue of credit ceilings, pointing out that credit ceilings were not an adequate solution as they would ration the credit and increase the cost for consumers. She also pointed out that redistributive policies belonged to the sphere of social policies and should not be mixed with consumer protection in the credit market.

Participants were interested to know how the Commission foresees the role of credit bureaus in the risk assessment, also for the case of revolving credit and cross-border operations. Jens Ring pointed out that Commission has not an a priori approach, but the consultation process will bring out the different practices in EU countries and from there will extract conclusions.

To clear some issues on the scope of the directive, Mr. Ring clarified that first, the Commission will consider national differences in the provision for individuals and professionals, as in some countries for instance, non-for-profit associations are covered consumer credit regulation. Concerning intermediaries, the intention is to make clear the competencies, “who is in charge of what”.

### **Session 2.**

#### **Rosa María Gelpi, Cetelem “A view from the industry”**

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Ms. Gelpi presented her views on the adequate approach to consumer credit regulation.

Ms. Gelpi based her speech on the debate among supporters of the different theories of harmonisation, namely, mutual recognition, host country, or maximum harmonisation. The debate between mutual recognition of country of origin regulation and host country regulation has been open for twenty years and general consensus has not been achieved.

The European Commission has tried to overcome the difficulties presenting different approaches for regulation before the contract and after the contract. However, she pointed out, in the long run only maximum harmonisation is desirable. The fact that for the time

being such approach is politically difficult, the Commission should not abandon long-term goals.

An effort is necessary to reach a sensible level of consumer protection that allows competition, which is ultimately advantageous for the consumer. Maximum harmonisation does not allow Member States to add provisions to European regulations, and therefore, simplify the operative environment for firms operating in the market and wishing to enter the market, contributing effectively to the completion of the single market.

Since on the supply side, markets are getting closer, countries converge economically, cultural barriers are erasing, shouldn't the regulatory framework in the different countries also converge?

### **Dominique Forest, BEUC "A view from the consumers associations"**

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Mr. Forest emphasised in his presentation the need for a revision of the consumer credit Directive since it hasn't had an impact on the comparability of European consumer credits. Two key issues to be approached in the new Directive should be intermediaries' role and indebtedness.

The cost of credit and the calculation of APR need further impulse from the European sphere. In this sense, he stressed that all costs, direct or indirect should be included in the calculation method, which should be the same in all the EU countries.

Contrary to the views expressed by Rosa María Gelpi, Mr. Forest is not in favour of maximum harmonisation, as it will diminish the existing level of consumer protection.

Regarding responsibility, the new Directive should consider an important re-balancing between credit and grantors. Grantors of credit should retain the responsibility on the ability of repayment, unless there are sufficient proof that they did enough assessment to avoid it.

Mr. Forest also expressed its concern on the scope of the future Directive, which given the importance of mortgage credit should also be included.

### **Samuel Theodore, Moody's Investor Service "US consumer and commercial finance companies in Europe: Climbing the learning curve"**

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Market saturation in the United States is prompting US finance companies to take an increased interest in European markets. A number of US finance firms have expanded into the UK and continental markets. US finance companies face several competitive challenges in Europe, namely the fragmentation of the market, in terms not only on the different expansion of products (credit cards, mortgages, saving products...), but in the fragmentation of national markets. Other factors are the less extensive use of credit loss

data, cultural differences or a less developed retail borrowing market. Additionally, consumer protection usury laws and data collection, just to name some, varies very much among EU countries.

Although credit markets are expanding in some European countries, US commercial finance companies can be expected to face different risks added to their operational or strategic risks, such as protectionist legislation and enormous differences in legislation within EU countries. US commercial finance companies moving into Europe should also note the lack of an integrated European retail credit market.

Finance companies have adopted different strategies to enter EU markets, some have entered the market “de novo” and build new firms, other have pursued acquisition or joint-venture approaches. Furthermore, poor or incomplete understanding of the national business and consumer culture will be a “perennial Achilles heel for companies seeking a foothold in these growing markets”.