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Comments

of the

**Zentraler Kreditausschuss and the
German Insurance Association**

**on the European Commission's modified proposal for a
Directive of the European Parliament and of the Council
on credit agreements for consumers amending Council Directive 93/13/EC
– Consumer Credit Directive**

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A. General remarks

The aim of reviewing the Consumer Credit Directive should be to enhance consumer protection and, in particular, find a solution to the problem of consumer over-indebtedness. Compared to the version of 28 October 2004, the draft presented by the European Commission on 7 October 2005 is generally a step in the right direction. Several sections take a more differentiated approach and contain rules which better reflect the realities of the lending business. We especially welcome the fact that the directive is now only to be applied to loan agreements of up to 50,000 euros and that mortgage credit is to be excluded from the scope. This will reduce regulatory requirements in certain areas. The exclusion of surety agreements from the directive's scope is also strongly supported.

We do not, on the other hand, agree with the Commission's proposed concept of "responsible lending". It cannot be the task of European legislators to attempt to protect the consumer from himself and give him the opportunity to shift the economic consequences of his actions onto his bank. In addition, the scope of the rules on "linked credit agreements" is too broad. The Commission's proposal therefore fails to apply its own concept of the responsible consumer. Furthermore, the information requirements to be imposed on the banks are still extremely bureaucratic and lack balance, as do the excessively broad requirements to provide advice. The creation of new liability for the banks risks giving rise to a situation in which banks become more cautious about extending loans, with the result that consumers of low credit standing will find it more difficult to access credit.

The Commission's draft also fails to provide a satisfactory solution to the question of how the directive's provisions are to be implemented in individual member states. In particular, it is unclear how the suggested combination of partial full harmonisation and minimum harmonisation with mutual recognition is to work in practice. It must be seriously doubted whether parallel application of such conflicting approaches in individual areas of consumer credit law will deliver the necessary level of legal certainty in practice.

B. Comments on individual provisions

I. Article 1 (subject matter)

The directive begins by indicating that it intends to harmonise only certain aspects of the rules and regulations governing consumer credit. Article 21 subsequently provides a rough indication of which parts of the directive are to be deemed definitive for national legislators in the sense of full harmonisation and which may be fleshed out with individual rules. Nevertheless, the directive fails to make it sufficiently clear to stakeholders and national legislators where exactly it is to be considered binding and where member states are to be allowed discretionary leeway. There is consequently a need to spell out more clearly than at present whether individual provisions are intended to be binding or not. Please also see our comments on Article 21.

II. Article 2 (scope)

The Commission's proposal pursues the tried and tested approach already adopted by the existing directive in the version of 22 February 1990 (90/88/EEC OJ L 61/14 of 10 March 1990) of excluding from the scope of the directive areas where there is no need for regulation or whose special nature requires them to be dealt with separately. The European Commission has quite rightly excluded mortgage loans, for example, since it is currently being examined in the context of the Green Paper on Mortgage Credit in the EU whether loans of this kind are in need of any further regulation at all. The German banking industry therefore supports the envisaged exclusion from the scope of the directive of the types of credit agreement listed in Article 2(2)(a) to (k).

1. Need for an exemption for very small loans

It does not, on the other hand, reflect market realities to refrain in Article 2(4)(a) from excluding very small loans altogether and instead propose that only some of the directive's provisions should apply to agreements involving amounts of up to 300 euros. Under Article 2(4), sentence 1, loans of this kind will be subject, for example, to the pre-contractual information requirements of Article 6 and to most of Article 9's requirements concerning information that must be included in the credit agreement. These information requirements alone – irrespective of the fact that they are fewer than those applying to other loans covered by the scope of the directive – go too far and would be unworkable in practice. Given the small

sums involved and the fact that this market segment is already difficult for the banks from a commercial point of view, even the “simplified” information requirements envisaged by the directive and the associated processing time and costs would be out of all proportion to the possible return. The increase in costs triggered by these requirements would ultimately have to be borne by the consumer, which would make small loans disproportionately expensive. What is more, the new information requirements would result in so much associated red tape that many banks would probably stop extending very small loans altogether. This would make access to credit more difficult, particularly for those sections of the population which currently take out very small loans of this kind. There is nothing new about these arguments. Article 2(1)(f) of the existing directive in the version of 22 February 1990 therefore quite rightly totally excludes from its scope “credit agreements involving amounts less than 200 ECU”. There is no evidence that this exemption has given rise to problems in the past. The current exemption for very small loans should therefore be retained when the Consumer Credit Directive is revised. And just as the maximum amount has been adjusted in Article 2(2)(b) of the proposal from the present 20,000 ECU to 50,000 euros, the current minimum threshold of 200 ECU should be raised to 500 euros.

2. Article 2(f) (credit agreements granted by an employer to his employees)

The proposed directive envisages an exemption in Article 2(2)(f) for loans granted by an employer to his employees. This definition is too narrow. In practice, employers normally offer loans of this kind not only to their own employees, but also to the employees of companies with which they are closely associated, by means of shareholdings, for example, or a co-operation agreement. The rule currently proposed by the Commission would result in employers being able to grant the type of loan in question only to employees working for them directly. In contrast, employees who had a special relationship with the “employer” offering the low-interest loan because of an outsourcing contract, co-operation agreement or shareholding arrangement would be excluded in future under the present wording. To avoid this, the exemption should be reworded as follows:

(f) credit agreements which are granted by an employer to his employees or the employees of associated or co-operating companies ... free of interest or at annual percentage rates of charges lower than those prevailing on the market;

3. Article 2(k) (exemption for promotional loans)

It is in principle to be welcomed that Article 2(k) envisages excluding promotional loans from the scope of the directive. The special nature of this type of credit has now largely been accommodated. The current wording is too narrow, however, and not always sufficiently precise.

- a) Firstly, the exemption is too narrow because it fails to consider that promotional loans are not always offered at reduced rates of interest. Preferential terms can also take other forms, such as waiving the need to provide collateral.
- b) Furthermore, the wording proposed by the Commission refers only to “creditors” which themselves fulfil “a statutory duty with a general interest purpose”. In practice, however, promotional loans are not only extended directly by promotional banks. It is far from unusual for a promotional bank not to extend the loan to the borrower directly, but for the promotional loan to be granted by a “usual” financial institution, though on terms prescribed and imposed by the promotional bank.

In practice, it may depend upon chance whether a promotional loan is granted by a promotional bank direct or by a “usual” financial institution on terms specified by a promotional bank.

In order to cover both loans extended indirectly under a public promotional scheme (see above under b)) and promotional loans which, though not offered at reduced interest rates, are nevertheless extended on preferential terms of some other kind (see above under a)), the exemption in Article 2(k) should be worded clearly and succinctly as follows:

credit granted to carry out state-promoted purposes (promotional loans).

4. Article 2(2)(i) and Article 2(4)(c) (loans which provide for the consumer and creditor to agree on arrangements concerning deferred payment or repayment methods)

Article 2(2)(i) rightly envisages excluding from the directive’s scope credit agreements “which relate to the deferred payment, free of charge, of an existing debt”.

Under Article 2(4)(c), in contrast, other arrangements concerning deferred payment or repayment methods are to fall within the scope, even if “the consumer would not thereby be subject to less favourable terms compared to the initial credit agreement”.

This distinction is not justified and will cause problems in practice – to the detriment of the borrower. A situation may arise during the lifetime of the credit agreement or when the loan matures in which the borrower is temporarily unable to meet his obligations owing to a short-term lack of liquidity, for example. Under existing law, it is possible temporarily to suspend the borrower’s payment obligations by concluding a debt deferral or repayment agreement without this involving any additional bureaucratic hurdles.

Aside from the fact that he naturally has to continue paying maturity-related costs on the amount he owes during the period of deferral under such an arrangement (i.e., in particular, interest), the borrower does not normally incur any further costs. The borrower is consequently not made subject by the arrangement to less favourable terms compared to the initial credit agreement – except that his maturity-linked costs (particularly interest) continue to fall due. The European Commission’s proposal to impose additional formalities on debt deferral or repayment agreements of this kind under Article 2(4)(c) will make it more difficult for banks to offer the unbureaucratic assistance outlined above. Yet there is no need to impose Article 2(4)’s additional information requirements on these agreements because the maturity-related costs (particularly interest) will not change for the period of the debt deferral or repayment agreement compared to those in the original contract and the borrower will have been fully informed of them before the latter was concluded. To enable debt deferral or repayment agreements which do not subject the borrower to less favourable terms than the original agreement to continue being concluded unbureaucratically, such agreements should continue to be excluded from the scope of the directive.

The exemption in Article 2(2)(i) should therefore be worded along the following lines:

- (i) *credit agreements which relate to the deferred payment, free of charge, of an existing debt and credit agreements which relate to deferred payment or repayment methods as long as the consumer would not thereby be subject to less favourable terms compared to the initial credit agreement except for the maturity-related costs arising from the longer life of the loan or costs arising from legal obligations such as the payment of default interest;*

In contrast, debt deferral or repayment agreements which make the consumer subject to less favourable terms compared to the original contract in a manner going beyond that outlined above should have to comply with the directive's full general information requirements. The partial exemption currently envisaged in Article 2(4)(c)(i) to (ii) could then be dropped.

III. Article 3 (definitions)

1. Article 3(d) ("overdraft facility")

Article 3(d) defines an "overdraft facility" as "a credit agreement whereby a creditor grants to a consumer the possibility to dispose of funds in his current account ...". This definition is too narrow and evidently assumes by using the term "funds" that there will normally have to be a credit balance on the account. This is often not the case and must not be a prerequisite for granting an overdraft facility. The definition should therefore be worded as follows:

(d) "overdraft facility" means a credit agreement whereby a creditor grants to a consumer the possibility to dispose of funds in his current account ~~which exceed the current balance in that account~~ as far as he has been granted a credit line and where ..."

2. Article 3(e) ("credit intermediary")

The term "credit intermediary" is defined in Article 3(e) as a person acting "on behalf of the creditor". Articles 19 and 20 subsequently set out the obligations of credit intermediaries on the basis of this definition and require member states to regulate them. The definition of credit intermediary is too narrow, however. In practice, loans are offered to consumers not only by persons working "on behalf of" the creditor, but also by a number of persons acting independently and who may well not receive a fee from the lending bank. There is no reason whatsoever to accord this category of intermediary privileged treatment. On the contrary, it is essential that these intermediaries also be subject to the requirements in Articles 19 and 20. The existing qualification in Article 3(e) should therefore be dropped and the definition worded as follows:

(e) "credit intermediary" means a natural or legal person who ~~on behalf of the creditor~~ ~~and~~ for a fee;"

3. Article 3(f) (“total cost of the credit to the consumer”)

- a) According to Article 3(f), the total cost of credit to the consumer – and thus also the annual percentage rate of charge under Article 3(g) – is to include “any kind of fees”. Yet the calculation of the total cost of credit and the annual percentage rate of charge should not include the cost of operating the current account which is used to effect payments. These costs are not currently reflected in the annual percentage rate of charge. For clarification purposes, the following sentence should be added to the definition in Article 3(f):

The costs of operating a current account which the consumer uses to effect payments are not to be included.

The cost of operating a credit account dedicated exclusively to processing and servicing the loan, on the other hand, must be included in both the total cost of credit and the calculation of the annual percentage rate of charge.

- b) Article 3(f) uses the wording “costs relating to ancillary services relating to the credit agreement”. Given that the objective of the annual percentage rate of charge (APRC) is to allow the costs of loans to be compared with one another, this is an unjustified extension of the definition. If costs are to be comparable, they must be based on the same or at least comparable elements. This is not the case under the present wording of Article 3(f). If the cost of an endowment insurance policy concluded in connection with a credit agreement had to be included in the APRC, this would mean different sets of circumstances would be compared with one another, i.e. credit agreements which did not require an endowment policy to be taken out and credit agreements which did. An endowment insurance policy is a service independent of the fate of the credit agreement, however. It is a means of accumulating capital and offers the policyholder protection against risk independent of the fate of the loan agreement. The consumer obtains an additional service compared to a borrower who does not take out an endowment policy.

If such costs had to be included in the APRC despite the arguments outlined above, they could theoretically only be the costs of covering risk and handling charges. The part of the insurance premium representing the savings portion of the insurance policy, in contrast, is not part of the costs that directly affect the cost of the loan. Unlike interest payments, for example, this savings portion of the insurance premium is not “used up”

during the lifetime of the loan, but accumulates to the benefit of the customer. However, it would be impossible or at least disproportionately onerous to split the covering risk from the overall insurance premium. In consequence, a Federal Court of Justice ruling of 18 January 2005 (WM 2005, 415 ff.) rejected this idea as impracticable.

Where instalment loans are concerned, moreover, it would only be possible to calculate the APRC or “total cost of the credit” on the basis of fictitious data since the life of the insurance policy will normally be longer than the fixed interest period of the loan at the end of which repayment will become due. And even with credit agreements which do not take the form of instalment loans, the variable amount of profit generated by the insurance would mean the calculation of the APRC or the “total cost of credit” would be based on at least partially fictitious data. Using the “safe” guarantee interest rate as the basis of calculating the effective rate of interest, on the other hand, would mean quoting the customer an effective rate of interest which in all probability was not accurate.

It is therefore not appropriate – as underlined by the above mentioned Federal Court of Justice ruling – to include expenditure relating to a savings programme in the costs used to calculate the annual percentage rate of charge.

We consequently suggest amending the wording of Article 3(f) as follows:

(f) “total cost of the credit to the consumer” means all the costs, including interest, commissions and any kind of fees which the consumer has to pay in connection with the credit agreement in conformity with the terms thereof, and which are known to the creditor; costs relating to ancillary services relating to the credit agreement, ~~in particular insurance premiums,~~ – in the case of insurance only premiums for insurance policies whose sole objective is repayment to the creditor in the event of realisation of the insured risk – are included if the conclusion of the service contract is compulsory for obtaining the credit or the advertised interest rate, (...)

This would ensure that the annual percentage rate of charge included only the costs of products which directly benefited not only the consumer, but also the loan agreement and the creditor, such as mandatory residual debt insurance, for example.

4. Article 3(1) (“linked credit agreement”)

In its present form, the definition of linked credit agreement proposed by the Commission is highly problematic, would expose the banks to far-reaching and incalculable liability risks and threatens to make banks much more cautious about granting consumer loans.

Though the wording of Article 3(1) is to a certain degree based on the provisions in Section 358 (3) sentences one and two of the German Civil Code, the actual impact of the definition proposed by the European Commission would go far beyond these.

a) Need for the definition to be more precise

Under Article 3(1)(ii) a “commercial unit” between the credit agreement and the financing agreement – i.e. a linked credit agreement – will always exist if the financing bank and the company selling the goods or providing the service are two different entities and the bank uses the services of this company “in connection with the conclusion, or preparation, of the credit agreement”. On the basis of this definition, every connection of any kind between the company and the credit agreement would result in the credit agreement being classified as a “linked credit agreement”. A mere mention by a company of a possible method of financing the goods or services would, under the proposed definition, qualify the credit agreement concluded by the consumer as a “linked credit agreement” – even in the absence of any legal relationship whatsoever between the financing bank and the supplier of the goods or services and even if the supplier was not brokering the loan on behalf of the bank. The definition proposed by the Commission in Article 3(1)(ii) is therefore all-encompassing and would bring the banks incalculable risks.

In Germany, the legal definition of “linked agreement” in Section 358 (3) sentence two of the German Civil Code – on which the definition in Article 3(1)(ii) is based – has been clarified by supreme court rulings. As things stand, a linked credit agreement may be deemed to exist only if the following condition is satisfied in addition to those mentioned in Section 358 (3) sentence two of the German Civil Code. There must be more than a simple means-to-an-end relationship between the financed goods or services and the credit agreement; the two agreements must be so closely connected with one another that neither would have been concluded without the other and each achieves its purpose only with the conclusion of the other contract (cf. decision of the Federal Court of Justice in BGH NJW 2000, 3065, 3066 and,

as one of many examples, the academic legal commentary by Habersack in *Münchener Kommentar zum Bürgerlichen Gesetzbuch*, 4th edition, Section 358 par. 36).

It is absolutely essential to avoid a situation where, in the process of adopting the definition from Section 358 (3) sentences one and two of the German Civil Code, the above clarification by supreme court rulings “goes astray” and an “abbreviated” version of the term “linked credit agreement” in EU law gives rise to an indiscriminate extension of the definition far beyond that existing under German law and a massive increase in the liability to be borne by the banks.

The definition in Article 3(l) must therefore first be made more precise. This could be achieved by adding the following underlined wording to the definition in Article 3(l)(i):

(i) the credit in question serves exclusively to finance an agreement concerning the supply of goods or the provision of a service and the two agreements are connected with one another in a manner beyond a means-to-an-end relationship so that neither agreement would have been concluded without the existence of the other and each achieves its purpose only with the conclusion of the other agreement and

(ii) ...

b) Need to delete the last clause of Article 3(l)(ii)

Under the definition in Article 3(l)(ii) currently proposed by the Commission, a “linked credit agreement” will also be deemed to exist “if the credit agreement makes reference to the specific goods or services to be financed with the credit”. For this reason, too, the definition would have incalculable implications and be unworkable in practice. A credit agreement is never an end in itself but is always concluded for the purpose of financing certain goods or services. But the mere fact that the goods or services are being financed cannot be held to mean that the credit agreement thus concluded is a “linked credit agreement”. Otherwise, all credit agreements concluded by consumers would have to be categorised as linked agreements and the banks providing the financing would be faced with incalculable liability risks. The special legal consequences and liability risks of a “linked credit agreement” arising from the definition in Article 3(l) in conjunction with the list of requirements in Article 14 must be triggered only under narrow, precisely defined conditions.

It is, moreover, common practice when extending credit to ask the borrower why he wishes to take out a loan and enter the reply on the credit agreement form – in a column marked “intended use”, for example. A reference of this kind to the intended use is, however, no meaningful indication as to whether the credit agreement and the financed transaction are “linked credit agreements” and form such a close commercial unit as to justify cancellation of the latter leading to automatic cancellation of the former as envisaged by Article 14(1).

Prudential considerations also argue against the proposed rule. Banking supervision law requires various types of credit agreements – both with consumers and with corporate customers – to show the intended purpose of the loan. In the context of monitoring credit risk, for example, banks in Germany are obliged by No. 51 of the “Minimum requirements for the credit business of credit institutions” (MaK) (Circular No. 34/2002 of 20 December 2002 of the Federal Financial Supervisory Authority/BaFin) to check whether borrowers use the funds extended to them for the purpose intended. A requirement imposed on a bank by its regulators to monitor whether or not a loan is actually put to its intended use cannot be allowed to result in all credit agreements that indicate the intended purpose of the loan suddenly becoming linked agreements. Nor does a reference to the purpose of the loan which is included to comply with banking supervision law provide any indication of whether the credit agreement and the financed transaction are linked agreements in terms of civil law.

The view expressed by the Commission in the final clause of Article 3(1)(ii) that a mere reference in the credit agreement to the goods or services is enough for it to be deemed a “linked credit agreement” is therefore based on a misconception.

The final clause in Article 3(1)(ii) worded

or if the credit agreement makes reference to the specific goods or services to be financed with the credit

must therefore be deleted.

c) No application of the rules on linked credit agreements to the loan-financed purchase of shares, derivatives and other financial market instruments subject to the fluctuations of the capital markets

Although the Commission's proposal has adopted rules on linked credit agreements which are to a certain degree based on German civil law, one important point has been forgotten. German law explicitly exempts application of the rules on linked credit agreements if the credit is used to purchase shares, derivatives or other financial instruments which are subject to the fluctuations of the capital markets (see Section 491 (2) (2) of the German Civil Code). It is essential that the EU Directive also include a rule of this kind. Otherwise, the consumer would be able to speculate on the financial and capital markets at his bank's expense. The following provision should therefore be added to Article 3(1):

(iii) The provisions on linked credit agreements do not apply if the credit agreement serves to finance the purchase of securities, foreign currency, derivatives, fund units, precious metals or other financial market instruments which are subject to fluctuations in the capital markets.

IV. Obligations to provide information and advice

The Commission's new proposal makes a distinction between four different types of information to be provided to consumers:

- Standard information for advertising (see also our comments on Article 4)
- Pre-contractual information (see also our comments on Articles 5 and 6)
- Information that must be included in credit agreements (see also our comments on Article 9)
- Advice provided by “explaining the pre-contractual information” (see also our comments on Article 5(5))

Irrespective of any reservations we may have about the content of specific information requirements, this multi-phase cascade of information with sometimes diverging and uncoordinated requirements is excessive. The proposed flood of data would result in overlaps, repetition and contradictions. Few consumers would be able to absorb, differentiate between and evaluate the various items of information of varying degrees of detail at each level. The aim of enabling the consumer to make an informed decision would be undermined.

While Article 4 should be deleted – see our comments below in Section IV 1. – it is at least a positive development that the final sentence of Article 5(2) allows banks to satisfy the pre-contractual information requirements of Article 5(2)(a) to (m) by supplying borrowers with a draft credit agreement containing the mandatory information to be provided in accordance with Article 9. Nevertheless, both the list of pre-contractual information required under Article 5(2)(a) to (m) and the list of mandatory information to be included in a credit agreement under Article 9(2)(a) to (o) contain various items which would unnecessarily formalise the granting of loans and erect additional bureaucratic barriers. This would significantly hamper lending business in practice – to the detriment of the consumer. Since the content of the rules in Articles 5 and 9 essentially refer to the same credit agreement, they will be analysed below in parallel.

1. Article 4 (standard information for advertising)

The European Commission's proposals in Article 4 for regulating the advertising of credit agreements are excessive, in our view, and would unreasonably restrict the promotion of loan products.

One example of an unjustified restriction – particularly compared to policy applying in other sectors – is the envisaged rule that certain information about the credit agreement must be presented in the order indicated in Article 4(2)(a) to (e). Furthermore, Article 4(2)(a) to (e) and Article 4(3) to (5) would require much of the pre-contractual and contractual information regulated in Articles 5 and 6 of the proposal – which is intended to be supplied to the consumer before or when the agreement is concluded – to be included even in an advertisement for a loan product. This is not practicable.

In their new *Directive 2005/29/EC of 11 May 2005 on unfair business-to-consumer commercial practices in the internal market*, the European Parliament and the Council recently adopted “uniform rules at Community level which establish a high level of consumer protection” that have approximated “the laws of the Member States on unfair commercial practices, including unfair advertising”. Article 3(9) of this directive explicitly leaves it to member states to decide whether or not to introduce separate requirements in the field of “financial services”. Aside from the fact that the approach adopted in Article 4 of the proposed Consumer Credit Directive is thus clearly at odds with the objective of Directive 2005/29/EC, the highly prescriptive rules in this article would be virtually unworkable in practice. Take, for

example, the mandatory specification of “the amount, number and frequency of payments to be made” under Article 4(2)(d) and of “any kind of fees in connection with the credit agreement” under Article 4(2)(e). This information alone – without even considering the other requirements envisaged in Article 4 – would be so extensive as to seriously hamper the banks’ ability to advertise their products, particularly compared to the requirements applying to other sectors of the economy under Directive 2005/29/EC of 11 May 2005. In the field of radio and television advertising, the Commission’s envisaged rules would be totally unfeasible.

Article 4 should therefore be dropped.

2. Article 5 (pre-contractual information) and Article 9 (information that must be included in credit agreements)

Before going into details concerning the pre-contractual information and information that must be included in credit agreements, we would like to make the general point that the information requirements envisaged in the Consumer Credit Directive are by no means always consistent with those in other EU directives, particularly the Distance Selling Directive for Financial Services. Furthermore, it is an open question how the sometimes diverging information requirements in various directives are meant to interact with one another. In the interests of legal certainty, no conflict must be allowed to arise from differing information requirements in different directives. The list of information requirements needs to be revised with this in mind. In addition, we have the following comments on various specific requirements currently envisaged:

a) Annual percentage rate of charge (Article 5(2)(d) and Article 9(2)(e))

The examples of calculating the annual percentage rate of charge contained in Annex II of the previous draft proposal for a revised Consumer Credit Directive have now been dropped. Instead, the banks are to be required under Article 5(2)(d) to provide “a clear and concise description” of the annual percentage rate of charge and the total cost of the credit to the consumer by means of a “representative example mentioning all the financial data and assumptions used for calculating this rate.” First of all, the “financial data and assumptions” referred to in this subparagraph will include factors influencing the bank’s pricing and business policy – i.e. confidential internal matters that do not need to be disclosed for competitive reasons. What is more, we believe it would not be helpful – even in the interests of transparency – to confront the borrower either before or on signing a contract with financial

mathematical and economic data of this kind (i.e. “all the financial data and assumptions used for calculating [the] rate”). Even a consumer with a background in financial mathematics and business economics would be unable to understand and evaluate “all the financial data and assumptions used for calculating that rate”, as it is worded in Article 9(2)(e).

aa) In Article 5(2)(d), therefore, the final phrase

by means of a representative example mentioning all the financial data and assumptions used for calculating this rate

should be deleted.

bb) The corresponding provision in Article 9(2)(e) concerning the annual percentage rate of charge with the slightly different wording but identical intention:

all the financial data and assumptions used for calculating that rate shall be mentioned

should also be deleted.

cc) Article 5(2)(h) uses the term “ancillary service” and refers to its relationship to the “advertised interest rate. Article 5(2)(d) stipulates that the consumer must be informed of the “annual percentage rate of charge” and the “total cost of the credit”. To clarify the relationship between these two provisions, particularly in cases in which the ancillary service is not compulsory (see also the definition in Article 2(f) and (g)), the following wording should be added to Article 5(2)(d):

The portion of the annual percentage rate of charge relating to an ancillary service may be itemised separately.

**b) Obligation to provide a “payment schedule”
(Article 5(2)(e) and Article 9(2)(f), (g) and (h))**

Under Article 5(2)(e), the pre-contractual information provided to the borrower should include the amount, number and frequency of payments to be made, “where possible set out in a payment schedule”. Article 9 on information for mandatory inclusion in credit agreements

contains a corresponding provision in paragraph 2(f), (g) and (h) also requiring the borrower to be given a “payment schedule”.

As the wording of Article 9(2)(f) makes clear (the payment schedule is to be provided only “where possible”), the European Commission correctly assumes that it will not be feasible to draw up a payment schedule for a number of loan products. This applies, for example, to all loan products where the borrower can draw on the funds made available to him as and when required in one or more instalments, possibly of differing amounts, and also to all revolving lines of credit. A statutory requirement calling on banks to prepare payment schedules “where possible” would thus merely create uncertainty in practice and be totally unhelpful for those trying to implement the rules.

Furthermore, the borrower already has to be informed of the “amount, number and frequency of payments” and is thus quite clear about what charges he will face each month. Given that both the pre-contractual and contractual information rules (see Article 5(2)(b) and (d) and Article 9(2)(c) and (e) respectively) require that he be advised, in addition, of the “total amount of the credit” and the “total cost of the credit”, the borrower is already fully informed about the monthly charges and the aggregate cost of the loan. There is consequently no need to introduce a requirement for a payment schedule. Use of such schedules is not currently common practice and the associated administrative costs would make lending more expensive.

aa) In Article 5(2)(e), the final phrase

where possible, set out in a payment schedule

should therefore be deleted.

bb) The corresponding provisions in Article 9(2)(f) to (h) requiring the supply of a payment schedule should also be deleted.

c) Costs payable to persons other than the creditor (Article 5(2)(g), (i) and Article 9(j))

The draft Consumer Credit Directive begins in Article 9(2)(e) in conjunction with the definition in Article 3(f) by correctly assuming that the “total cost of the credit to the consumer” quoted by the bank should include only “all the costs” which the consumer has to pay in connection with the credit agreement to the bank. Under the legal definition in

Article 3(f), “costs relating to ancillary services” payable to third parties must be reflected in the total cost of the credit to the consumer and the annual percentage rate of charge only if the bank makes the conclusion of an additional agreement, such as an insurance policy, a mandatory condition for granting the loan or the advertised interest rate. Up to this point, the Commission’s proposed concept for calculating the total cost of the credit to the consumer and the annual percentage rate of charge is coherent and correct.

- aa)** The rule in Article 5(2)(g) then envisages that the borrower must also be advised of all further “costs payable by the consumer ... to persons other than the creditor or the credit intermediary”.

Banks normally have no knowledge, however, of what costs will be charged to the consumer by “a notary or tax authorities”, for example (these costs are explicitly mentioned in Article 5(2)(g)).

Article 5(2)(g) consequently demands the impossible and must therefore be deleted.

- bb)** Article 5(2)(i), which envisages that the borrower should be advised of “interest in the case of overdue payments” and “charges for defaulting”, would also be unworkable in practice. Costs and “charges” of this kind are incurred only if the consumer fails to honour his contractual obligations, particularly his financial obligations, or fails to do so promptly. The question of what loss will then be incurred by the bank or, as the draft directive puts it, what “costs” or “charges” the borrower will have to pay for failing to meet his contractual obligations cannot be answered at the time the agreement is concluded and no figure can be put on the amounts involved. This is because the amount the borrower will be asked to pay in the event of him violating his contractual obligations is determined, among other things, by the length of time and the extent to which he fails to make the repayments and (particularly if a variable-rate loan is involved) by the interest rate applicable at the time he fails in part or in full to honour his contractual obligations. Any attempt at the time the agreement is concluded to put a figure on the costs the borrower would incur should he fail to meet his contractual obligations at some point in the future would therefore be totally arbitrary, provide the consumer with no meaningful information and be highly misleading. The bank’s obligation to indicate “costs” can thus – in line with the definition of “total cost of the credit to the consumer” in Article 3(f) and the calculation of the annual percentage rate of charge under

Article 3(g) on which this is based – refer only to costs which will be incurred if the borrower acts in accordance with the contract.

Article 5(2)(i) must therefore be deleted.

cc) The corresponding rule in Article 9(j) on information for mandatory inclusion in the credit agreement must also be deleted. This is worded slightly differently from the provisions in Article 5(2)(g) and (i), but the effect is the same. Like Article 5(2)(g), it envisages advising the consumer not only of the “total cost of the credit” which will be used to calculate the annual percentage rate of charge within the meaning of Article 3(f) and (g), but also of all “costs ... which are not included in the calculation of the annual percentage rate of charge”, i.e. also costs payable to third parties. As pointed out above, however, the bank has no influence on such costs. It has no knowledge of the amounts involved and will sometimes not even be aware of the reason for the costs. As to the idea of indicating the “interest in case of overdue payments”, “interest on arrears”, etc. at the time the agreement is concluded, our comments above under bb) on Article 5(2)(i) apply here, too.

d) Indication of the costs of early repayment and the method used to calculate them (Article 5(2)(l) and Article 9 2(n))

Even if the borrower were to be given the right to repay the loan principal at any time and in the absence of a compelling reason (which would lack all justification – see our comments on Article 15 for details), the bank would still have no way of informing him at the time the agreement is concluded of what “costs” he would incur in the event of premature repayment. Regardless of whether a fixed-rate or variable-rate loan is involved, the amount to be paid by the borrower in the event of early repayment depends first and foremost on the rate of interest specified in the contract and the prevailing interest rate at the time the principal is repaid prematurely. Only by applying these parameters is it at all possible to calculate the amount of “a fair and objective indemnity”, as Article 15 puts it. Since the future development of interest rates and thus the amount of the indemnity to be paid to the bank in the event of early repayment is not known at the time the contract is concluded, it is impossible to indicate the associated costs in the credit agreement.

aa) The rule in Article 5(2)(l) must therefore be deleted.

bb) The corresponding rule in Article 9(2)(n) on information for mandatory inclusion in the agreement, which is worded slightly differently but whose content is the same, must also be deleted.

3. Article 5(1) (requirement to assess the consumer’s creditworthiness and principle of “responsible lending”)

a) No civil law requirement for the bank to assess the creditworthiness of the borrower

With Article 5(1), the European Commission makes the obligation to check a borrower’s creditworthiness before granting a loan – a requirement already imposed on banks by their regulators, i.e. under public law – an independent civil law obligation in the context of “responsible lending”. This thus creates a new circumstance giving rise to liability at the banks’ expense. It will enable the consumer, in the event of no longer being able to repay the loan, to bring an action for damages against his bank and claim that it is responsible for the default because it failed to assess his creditworthiness adequately. By arguing in this way, the borrower could potentially clear himself of any obligation to repay the loan. Such an arrangement is blatantly at odds with the principle that it is the consumer himself who must ultimately – and naturally on an informed basis – decide whether or not to take out a loan. It cannot be the task of European legislators to try to protect the consumer from himself. Nor should the consumer be allowed to shift responsibility for his actions onto his bank. But the European Commission is proposing to give consumers the legal mechanism to do precisely that. Creating additional circumstances giving rise to liability for the banks would, moreover, inevitably result in banks becoming much more cautious in their lending. This would make it especially difficult for consumers with a low credit standing to access loans.

The obligation to check the creditworthiness of the consumer must remain a matter of banking supervision law alone and must not be allowed to become a basis for civil law claims for damages by the borrower against his bank. Article 5(1) should therefore be deleted in its entirety.

b) Information to be provided by the consumer

It is true that the Commission’s new proposal assumes there will be an exchange of information between the two parties before the agreement is concluded. Nevertheless, unlike

the second report by the European Parliament's Committee on Legal Affairs and the Internal Market¹, which envisaged information requirements for both sides, the Commission's proposal imposes specific obligations only on the bank.

The consumer's duty to provide information to the bank, on the other hand, is not spelled out sufficiently clearly. It is alluded to only indirectly in connection with the creditor's obligation to assess the consumer's creditworthiness "on the basis of accurate information provided by the latter". It is not specified, however, exactly what information the consumer is expected to provide or whether he has a legal duty to disclose all relevant particulars. Even the requirement in Article 6(1) of the 2002 Commission proposal for the consumer to reply to the bank's questions "accurately and in full" has now been dropped.

To maintain a balance between the information requirements for both parties and avoid the risk that the consumer's duty to furnish information cannot be enforced, it must be spelled out what this duty entails.

Concrete information requirements to be met by the consumer should be enshrined in the text of the directive and should cover, in particular:

- exact address, date of birth, nationality, marital status and marital property arrangements,
- details of the type and length of any inability to work, name of employer and type of employment,
- details of the consumer's assets, with reference to the type, amount and legal basis of his income (e.g. from self-employed or employed activities, rent received, capital investments and any other regular income such as child allowance, etc.),
- details of any adults living in the household who are entitled to maintenance and any dependent children,
- details of his liabilities, with particular reference to the type, amount and legal basis of the liabilities (e.g. motor vehicle costs, insurance policies, maintenance payments, living costs, rent, maintenance costs of owned property, social security payments, savings plans, liabilities from other credit agreements, leasing instalments, etc.).

¹ Second report, of 2 April 2004, on the proposal for a European Parliament and Council directive on the harmonisation of the laws, regulations and administrative provisions of the Member States concerning credit for consumers (A5-0224/2004).

It must also be borne in mind that the banks will not normally be able to consider all the eventualities which may have an impact on the consumer's ability to meet his contractual obligations. To enable the bank to make a decision about a loan based on consideration of the actual income and liabilities of the consumer, the directive must impose an explicit obligation on the consumer to disclose particulars of his financial situation, especially any liabilities which may not have been covered by the bank's questions and which are known only to the consumer.

4. Article 5(5) (explanation of the advantages and disadvantages of the products proposed)

The European Commission's proposal envisages four phases of information requirements. In addition to providing the information required under Articles 4, 5(2) and 9, banks must also give consumers "adequate explanations" about the proposed loan products, including their associated "advantages and disadvantages".

This requirement to provide borrowers with "adequate explanations" about "the advantages and disadvantages associated with the products proposed" before every single agreement is concluded imposes a general obligation on banks to provide information and advice which does not currently exist in this form. It will give rise to a considerable additional administrative burden, whose associated costs will have to be borne by all borrowers. The banks will have to document the type, content and extent of the information and advice supplied to every single borrower before concluding every single contract so that they will have evidence that can stand up in court in the event of the borrower subsequently claiming damages on the grounds that he was not adequately advised of the advantages and disadvantages of his loan. On top of this huge documentation and administrative burden, however, the banks will also face a much higher liability risk. If it turns out that the borrower cannot meet his contractual obligations, the Commission's proposed rule will enable him to claim a violation of Article 5(5) and sue his bank for damages.

Given that the Commission's proposed pre-contractual information requirements under Article 5(2) and information for mandatory inclusion in the agreement under Article 9 already constitute a comprehensive information regime, it would be unreasonable to introduce an additional obligation to provide general explanations and advice about the proposed products and their advantages and disadvantages.

Furthermore, the advantages and disadvantages of a credit agreement will always involve subjective aspects about which the bank cannot deliver a definitive assessment and which are not justiciable. We consider it absurd to expect, as indicated in Recital 20 of the proposal, that products should be explained to the consumer in a personalised manner. This would make it all but impossible to conclude consumer credit agreements on a cross-border basis using electronic media (see Article 9(1)), the facilitating of which is one of the objectives of the Consumer Credit Directive. The need to explain products to consumers personally and individually as required by Article 5(5) would, moreover, virtually rule out distance selling, which the Commission wishes actively to promote with the Distance Selling Directive for Financial Services.

It goes without saying that the consumer must be in a position to make an informed decision. This makes it absolutely essential for the relevant information to be made available to him in a comprehensible form. The banks will not, however, normally be able to go beyond this and analyse the customer's "needs" or motives for taking out a loan. The envisaged rule in Article 5(5) must therefore be deleted.

Only if a borrower approaches the bank with a concrete request for advice in connection with the credit agreement and is prepared to pay the associated additional costs is the bank naturally obliged to provide the customer with such specifically solicited advice. Even in this case, however, the bank cannot take the ultimate decision for the borrower about whether to take out a loan and, if so, which of the various types of credit agreement to select. If an obligation of this kind for the bank to provide advice on request and on a case-by-case basis is to be enshrined in the directive, Article 5(5) should be worded along the following lines:

Member States shall ensure that creditors and, where applicable, credit intermediaries, on the express wish of the consumer for advice concerning the proposed products, can conclude a separate advisory agreement under which they will provide the consumer, for a fee, with explanations about the proposed products, for example by explaining the pre-contractual information.

V. Article 6(1) in conjunction with Article 9 (credit agreements in the form of an overdraft facility)

Under Article 2(3) “credit granted in the form of an overdraft facility” on a current account is to be subject to a modified list requirements. According to the Commission’s explanatory memorandum, overdrafts are to be “submitted to a light regime only”². This is not reflected in the rules themselves, however. The envisaged rules for overdraft facilities therefore need to be amended.

1. Excessive information requirements

The Commission’s proposal envisages that overdraft facilities will trigger the following information requirements:

- first, standard information for advertising (see Article 2(3) in conjunction with Article 4),
- then special pre-contractual information requirements for credit agreements in the form of an overdraft facility (see Article 2(3) in conjunction with Article 6),
- followed by information that must be included in credit agreements (see Article 2(3) in conjunction with Article 9(2)(a) to (d), (h) and (o))
- and, finally, the list of information in Article 11, which must be delivered to the consumer “regularly”.

This does not measure up to the European Commission’s self-declared aim of introducing “a light regime only” for overdrafts. This applies even in view of the fact that Article 6(3) reiterates the mechanism set out in the final sentence of Article 5(2) and allows banks to satisfy the pre-contractual information requirements by supplying a copy of the draft credit agreement containing the information pursuant to Article 9(2)(a) to (d), (h) and (o) (see Article 2(3) of the proposal).

The existing Consumer Credit Directive contains a provision in Article 2(1)(e) exempting overdrafts on current accounts from the scope of the directive. There is no evidence, nor has the European Commission alleged, let alone demonstrated, in discussions to date that the present exemption has led to problems in the past. The proposed flood of information would make it impossible to continue making liquidity available simply and unbureaucratically by

² See par. 5.3.3. of the proposal’s explanatory memorandum.

granting an overdraft on a current account. The red tape required by the Commission would be out of all proportion to a possibly only temporary need to overdraw to honour to a direct debit for a utility bill, for example. The exemption for overdrafts on current accounts in the existing version of the directive must therefore be retained. The rule in Article 11 is sufficient.

2. Impossibility of indicating an annual percentage rate of charge for credit agreements in the form of an overdraft facility

Irrespective of the fact that the Commission's proposal imposes excessive requirements on the banks so that the exemption for overdraft facilities in Article 2(1)(e) of the existing Consumer Credit Directive should be retained (see above), some of the envisaged information requirements are totally impracticable. This applies, for example, to the requirement under Article 2(3) in conjunction with Article 6(1)(c) to indicate the annual percentage rate of charge on an overdraft and, what is more, provide "a representative example mentioning all the financial data and assumptions used for calculating that rate". Aside from the fact that it is totally unclear what a representative example of this kind is supposed to look like, practical considerations make it virtually impossible to describe in a transparent manner "all the financial data and assumptions" used for calculating the annual percentage rate of charge to a customer with no financial mathematics and business economics knowledge. Please see also our comments under IV. 2 a).

- a) It is interesting to note that the European Commission itself assumes in Article 2(3) that information about the annual percentage rate of charge cannot be provided for overdraft facilities. This paragraph, from which may be inferred what information "must be included in credit agreements", expressly omits the calculation of the annual percentage rate of charge under Article 9(2)(e) from the list of contractual information requirements. But if the annual percentage rate of charge is not an item for mandatory inclusion in a credit agreement in the form of an overdraft facility pursuant to Article 2(3) in conjunction with Article 9(2)(a) to (d), (h) and (o), it follows that the obligation in Article 6(1)(c) to provide the annual percentage rate of charge as one of the pre-contractual information requirements must also be deleted.
- b) Given that the annual percentage rate of charge does not have to be indicated under Article 2(3) in conjunction with Article 9(2)(a) to (d), (h) and (o) (see comments under a) above), the reference in Article 2(3) to Article 18, which regulates the calculation method for the annual percentage rate of charge, must also be deleted.

VI. Article 10 (information on the borrowing rate) – consideration of Basel II

The new Basel capital accord (Basel II) was published on 26 June 2004 and will be implemented in European law by amendments to EU directives 2000/12/EC (Codified Banking Directive) and 193/6/EEC (Capital Adequacy Directive). It aims, among other things, at ensuring that banks take greater account of the individual risk of default of their customers than was the case in the past. This prudential objective does not, however, guarantee in itself that an interest rate contractually agreed with a customer can be adjusted under civil law in the event of the creditor changing its rating of the borrower.

The European Commission has not taken account of this banking supervision development in its proposal for a revised Consumer Credit Directive. Since Basel II's regulatory requirements affect not only corporate customers but also the area of consumer credit, there is a need to clarify in Article 10 that a bank may adjust a fixed or variable interest rate in its contractual relationship with the borrower if it emerges in applying recognised prudential risk classification criteria (Basel II) that the customer's probability of default or the loss given default has changed.

VII. Article 12 (open-end and long-term credit agreements)

The European Commission has now included a rule in Article 12(2) on terminating open-end credit agreements. We would like to take this opportunity to point out that a rule of this kind is absolutely essential for prudential reasons and constitutes a basis for ensuring that banks can continue to offer both retail and corporate customers credit facilities, particularly in the form of credit lines on their current accounts. It is therefore vital for this rule to be retained in its present form. The background is as follows:

Under prudential rules applying to the entire European banking industry, a bank must set aside liable capital equivalent to 8% of all risk assets (including loans). In other words: a bank's scope for lendings is equivalent to 12.5 times its regulatory capital. Germany's Federal Banking Supervisor Office (BaKred), whose responsibilities have now been taken over by the Federal Financial Supervisory Authority (BaFin), issued numerous regulations on the application of capital adequacy rules. Under the terms of these banking supervisory regulations, banks have been permitted up to now not to apply, subject to certain conditions, the so-called "Principle I" (which spells out the above capital adequacy rules) to open-end loan commitments extended to retail and corporate customers for the purpose of providing liquidity.

Such loan commitments include credit lines and overdraft facilities granted on current accounts. However, BaFin's rules state that a prerequisite for this is that these "loans with no fixed term" may be terminated by the bank without notice as provided for in the General Business Conditions of Germany's private commercial banks and savings banks. If, on the other hand, a credit facility is agreed in a form that does not allow the bank the possibility of termination without notice, Section 8 (2) d) of Principle I stipulates that such credit facilities must be counted as off-balance-sheet transactions at 50% of their basis of assessment and backed by regulatory capital. The ability to terminate open-end credit agreements without notice consequently determines to what extent banks have to set aside regulatory capital for such credit lines. If European legislators withdrew the banks' ability to terminate credit agreements of this kind without notice, they would in future need to be backed by regulatory capital, both in the retail and corporate sectors. This would inevitably lead to a tightening of the amount of credit which the banks could potentially make available to retail and corporate customers. Article 12(2) must therefore be retained in its present form.

VIII. Article 13 (right of withdrawal)

- a) There are now a number of European directives which envisage informing the consumer about his right to withdraw from an agreement. As things stand, the Consumer Credit Directive does not clarify the relationship between its right of withdrawal and rights of withdrawal to be granted under other directives such as the Distance Selling Directive or the Doorstep Selling Directive. A situation must not be allowed to arise where the same consumer has to be informed about several rights of withdrawal. A provision must therefore be included in the Consumer Credit Directive clarifying that, if an agreement is concluded which requires the consumer to be informed about his right of withdrawal under several European directives, it is only necessary to provide the information once. In view of the fact that the directives involved may require different conditions to be satisfied for the period of withdrawal to begin – take, for example, the special rules when distance selling is involved – the Consumer Credit Directive also needs to clarify which criteria will trigger the start of the withdrawal period under which circumstances.
- b) The reference to paragraph 2 in Article 13(4) is incorrect. The first sentence should read:

Following the exercise of the right of withdrawal in accordance with paragraph 3, the creditor shall notify the consumer ...

IX. Article 14 (linked transactions)

The Commission's proposed rules on linked transactions would result in virtually unlimited liability for the banks, particularly due to the ill-defined and large impracticable definition in Article 3(1), and cannot be retained in their present form. It is therefore essential, first, to define this term, which determines the scope of Article 14(1), more precisely. For details, please see our comments under III.4. But the content of the rule in Article 14 itself is unclear, too. Since Article 14(3) leaves the fleshing out of the rules on linked transactions to national legislators, there is a lack of legal certainty about the implications of a cross-border linked transaction – particularly given Article 21's combination of potential full harmonisation, partial minimum harmonisation and the principle of mutual recognition. The proposed rules in Articles 14 and 21 are therefore not a suitable means of creating a reliable legal framework.

X. Article 15 (early repayment)

1. Article 15(1)

Under Article 15(1), the consumer is entitled to an “equitable reduction in the total cost of the credit”. Such a reduction must refer to costs that have not yet been used, however. Costs which have already been incurred and used, on the other hand, such as the fee for concluding the contract or evaluation fees for collateral, must be excluded and cannot be reduced or refunded. To make this clear, Article 15(1) should be reworded as follows:

In such cases, [the consumer] shall be entitled to an equitable reduction of the maturity-related total cost of the credit.

2. Article 15(2)

- a) The proposal envisages granting the borrower the right to repay the principal at any time irrespective of what was agreed in the contract and even in the absence of a compelling reason. Even if the exemption from the scope in Article 2(2)(a) means that this rule does not apply to loans secured by a mortgage, it constitutes serious interference in the civil law principle of “pacta sunt servanda”, which applies not only in Germany but in other European countries, too. In Germany, moreover, it also goes far beyond the borrower's rights of termination as enshrined in Sections 489 and 490 of the German Civil Code. Furthermore, banks are subject to detailed prudential rules on managing liquidity and

interest rate risk. The purpose of these rules is to ensure that a bank, taking into account the liabilities arising from its deposit-taking business and the income generated from lending operations, will always have sufficient liquidity at its disposal. Giving borrowers the right to repay their loans at any time without a compelling reason and, moreover, without paying an early repayment penalty (see below under b)) would constitute interference in these prudential liquidity and interest rate management mechanisms.

Quite apart from this, the Commission's proposal would mean it would no longer be possible to make a legally effective contractual agreement waiving termination rights for fixed-interest loans. The rule would effectively give the consumer an unconditional right of withdrawal from the credit agreement at any time – although the right of withdrawal is actually supposed to be limited to 14 days under Article 13 of the draft directive. If fixed-interest loans, which protect consumers from fluctuations in interest rates, had to be granted on these terms, the banks' readiness to offer consumers such loans would decrease sharply. A right to repay the loan at any time and in the absence of a compelling reason would most certainly change conditions for the worse from the consumer's point of view. Product diversity would be restricted on the loan market, as would the consumer's freedom of choice. What is more, the anticipated decline in fixed-interest loans would deprive consumers of effective protection against interest rate swings. A right to early repayment of the principal can only, if at all, be granted to the borrower for variable rate loans.

- b)** Furthermore, Article 15(2) envisages totally excluding the bank's entitlement to a fair indemnity for early repayment under certain circumstances. This is not justified. Not only German law recognises that the purpose of an indemnity is to compensate the creditor for the loss incurred as a result of the early repayment of the loan and put it in the position it "would have been in in the event of due performance of the credit agreement" (Section 249 of the German Civil Code)³. There is no discernible reason why the creditor should not be entitled to claim such an indemnity for a credit agreement "where the period used to fix the borrowing rate is less than one year", for example, as envisaged under Article 15(2)(a). The bank incurs a loss if the fixed interest period is less than one year in exactly the same way as it does when other fixed interest periods are involved. It is neither logical nor justifiable for this loss not to be compensated. The exemptions in Article 15(2)(a) and (b) should therefore be deleted.

³ Cf., for example, BGH WM 1997, p. 1747 ff. and the memorandum on the government draft of the Act to Modernise the Law of Obligations, Bundestag circular 14/6040, p. 254 ff.

XI. Article 16 (assignment of rights)

We unreservedly welcome the intention of the rule (already envisaged in the previous version of the proposal and now contained in Article 16), which aims at allowing banks to transfer the risk arising from a credit agreement. The actual wording of the article, however, contains an inaccuracy which distorts the intended meaning and must be eliminated.

Both Article 16 and Recital 27 are based on the concept that the consumer need be informed by the bank about the transfer of the credit risk only if the transfer to a third party affects the legal relationship between him and his bank. In all other cases, i.e. if the legal relationship between consumer and bank are not affected in any way because the bank remains the consumer's sole contractual partner even after the assignment, there should be no need to inform the consumer about the transaction since his legal position stays the same. This approach is to be welcomed.

The use of the term "for securitisation purposes" in both the article and the recital, however, fails to reflect what the European Commission wishes to achieve with this rule. Securitisation is only one of the methods used by banks to transfer credit risk. But it is neither necessary nor typical. A bank is just as likely to transfer the risk arising from a credit agreement without a securitisation transaction being involved. It is, moreover, totally irrelevant from the borrower's point of view whether or not a securitisation transaction is effected in connection with the assignment of the credit agreement or transfer of credit risk. The securitisation takes place outside the legal relationship between the borrower and the bank and does not affect the borrower's legal position vis-à-vis his bank with respect to the credit agreement. This linguistic inaccuracy must be eliminated.

1. Need to reword Recital 27

The intention of the rule could be reflected in Recital 27 as follows:

However, where the assignment is effected for the purpose of transferring the credit risk or for refinancing purposes only ...

2. Suggested wording for Article 16(2)

The objective outlined above and desired by the European Commission could be achieved with the following wording:

... except where the assignment is effected for the purpose of transferring the credit risk or for refinancing purposes only ...

XII. Article 17 (overrunning of the total amount of credit)

1. Article 17(1)

Under Article 2(3) in conjunction with Article 17(1), banks are required to provide borrowers who go over the overdraft limit on their current account with the information envisaged in Article 17(1) “in the event of a significant overrunning of the total amount of credit which exceeds a period of one month”. This approach is basically acceptable and practicable. Nevertheless, since the borrower will normally be informed about his overdraft facility within the meaning of Article 11 by means of the same medium as that used by the bank when informing him that the amount of credit has been exceeded, the wording of Article 17(1) should be adapted as follows to that in Article 11(1):

In the event of a significant overrunning of the total amount of credit which exceeds a period of one month, the creditor shall inform the consumer by means of a statement of account, on paper or on another durable medium ...

2. Article 17(2)

Article 17(2) envisages that “any significant overrunning of the total amount of credit which exceeds a period of three months shall be rectified, where necessary through a new credit agreement providing for a higher total amount of credit”. This would require the bank to check after every movement on a current account whether the credit limit had been exceeded and, if so, by how much and exactly when the three-month period had begun and would end. A new three-month period would have to be calculated based on every single entry on the account. This is not feasible. What is more, the introduction of a monitoring mechanism of this kind and the associated administrative work involved would make tolerated overdrafts so expensive that it is doubtful whether this unbureaucratic form of credit on a current account could continue to be offered.

Article 17(2) should therefore be deleted.

A further problem is that it is totally unclear when a "significant" overrunning of the total amount of credit should be deemed to exist under Article 17(1) and (2). Difficulties in application and of definition are therefore likely to arise when these rules are implemented in practice.

XIII. Article 21 (harmonisation, mutual recognition and imperative nature of the directive)

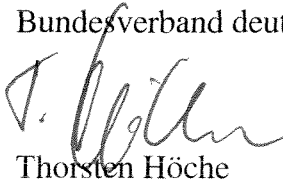
The approach adopted in Article 21 is unlikely to succeed in improving the legal environment for consumer credit in the European internal market. The combination of full harmonisation, minimum harmonisation and the principle of mutual recognition seems to be more of a theoretical legal concept. In practice, however, it would be largely unworkable since it is highly complex and raises the question in connection with every single provision as to whether a definitive rule exists or not. Furthermore, it is not always clear where the provisions mentioned in Article 21(2) leave room for national diverging rules and where the directive is to be considered definitive (e.g. Article 13 and Article 14(1)). This rule would result in considerable legal uncertainty when implementing the directive.

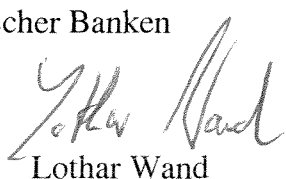
XIV. Article 26 (transitional measures)

The proposal in Article 26(2) for banks to adjust all open-end credit agreements throughout Europe within two years of the directive coming into force is out of touch with market realities. The total cost for the banks of having to modify a hundred million contracts would amount to billions of euros. What is more, revising existing agreements in this way would inevitably result in many agreements not being continued in their present form but having to be terminated or offered to consumers only on less favourable terms.

Article 26(2) should therefore be deleted.

Yours sincerely
for the Zentraler Kreditausschuss and
German Insurance Association,
Bundesverband deutscher Banken


Thorsten Höche


Lothar Wand