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The «Europeanisation» of credit supply and advice



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Like other financial services credit supply in Europe will be influenced by two developments likely to lead to «Europeanisation» or a genuine Single market in credit: these are the Euro and technological opportunities offered by e-commerce.

Due to the immaterial nature of financial services — there is nothing to wrap up in paper — marketing and payment via e.g. the Internet is exceptionally easy. Add to this the Euro, and the entire EMU becomes in principle one market.

It follows that these developments could give rise to an entirely new dimension for debt advice. It may be that, one day, a debtor may present at a German money advice centre looking for help with his Belgian financed mortgage, his English insurance policy and his Dutch removal bill.

Hence it has become essential for European debt advice agencies to work together, in order to learn from each other, to exchange information and to build an infrastructure which will enable the rapid communication of information to take place.

The two vectors, the Euro and e-commerce, also influence policy considerations at EU level.

This note will draw attention to an existing structure for co-operation between debt advisers, the Consumer DebtNet, CDN, and attempt to draw preliminary conclusions for EU policy on the prevention and cure of over-indebtedness.

1. Consumer DebtNet

Formed in 1994, CDN is a network of advisers to the general public on the problems and issues associated with the management of debt and handling/prevention of over-indebtedness. These advisers are employed in public services and by NGO's and the network includes members from all EU Member States as well as from the EEA states, Switzerland, Malta and the Baltic states.

The European Commission (represented by DG XXIV) has supported CDN activities since 1996. The Commission has encouraged CDN to develop towards a formal structure with a view to reinforcing its role as representative of the public and voluntary activities in the field of debt problems. For the Commission CDN constitutes one of the major actors in the policy development in this area.

CDN has the following basic aims and objectives:

- Organisation of the regular exchange of information;
- Organisation of training events;
- Planning and execution of joint European campaigns;
- Influencing European legislation and directives from Brussels;
- Identifying measures to improve the methodological basis of debt and budget advice;
- Development of improved preventative measures;
- Development of research initiatives and (joint) initiation of research;
- Organisation of annual conferences.

Since the summer of 1995, CDN has had its own English language magazine, entitled «Money Matters», which is an important source of information for European debt advice.

2. Conclusions for EU Consumer Policy

«Over-indebtedness» has many facets and is a complicated issue. The main causes are, however, clear: they are economic and social, namely unemployment and family breakdown



because of death, illness or divorce; following these causes is the incapacity to manage a budget.

These are not themes for consumer policy as traditionally understood although consumer education may help improve budget management capacities.

This view of the issue is not in itself fundamentally challenged by the opportunities for «Europeanisation».

Notwithstanding, pursuit of the classical consumer policy goal of protecting the economic interests of consumers, a goal recently confirmed as a key priority in the Consumer Policy Action Plan for the years 1999 to 2001, must inevitably touch upon over-indebtedness.

2.1. Prevention

It is, however, mainly on the prevention side that EU consumer policy can do something: the only existing legislative basis is the Consumer credit Directive 87/102 as amended. DG XXIV is currently carrying out a process of overhaul of and a number of areas in this legislation offer interesting opportunities for prevention:

Enhanced information

Attempts to harmonise in a positive manner the cost of credit have so far failed: Member States do not see scope for defining in a positive way which cost elements should be allowed when fixing the cost of a credit as indicated in the APR. Member States still prefer the current approach: a negative list, i.e. a list of exemptions.

Nevertheless, the drafting of these exemptions can no doubt be made. A good example is the exemption of insurance cost «unless these are mandatory»: Experience shows that these costs are often *de facto* mandatory in that the credit provider refuses to grant credit unless it is insured; but it is not necessarily the credit provider that offers the insurance and it is not stated formally in the credit agreement that insurance is obligatory so insurance cost is systematically excluded from the APR. One way out of this might be to delete the «mandatory» aspect and simply impose inclusion of indicative insurance cost.

Payment Protection Insurance

Should Payment Protection Insurance, PPI, be mandatory? If the main reasons for over-indebtedness are events — unemployment, death, divorce — there is a case for insuring against these systematically. Present experience indicates that the cost would be exorbitant. However, given i.a. that banks insist that only app. 2% of credit contracts give rise to repayment problems, it is difficult to understand this situation. No doubt insurance has been expensive; the point is that a mandatory scheme is likely to lead to market developments that would bring down these costs dramatically.

Debt registration

Debt counselling services often encounter cases where the income of borrowers was inadequate to repay even at the outset of the agreement. As credit providers carry out credit-worthiness assessments, credit scoring, such situations can hardly be characterised by any other term than irresponsible or reckless lending.

A radical solution to this problem is of course to make creditors totally liable or rather responsible for any losses they may incur following a credit provision transaction: in case of incapacity to pay or over-indebtedness it should be for the creditor to write off the loss, not for the consumer to enter into a repayment arrangement. However, this approach is as morally biased as approaches putting the blame exclusively on the debtor.

But more pragmatic approaches exist, namely debt registration that triggers obligations for credit providers. Credit registration can be either positive (as in the Netherlands), i.e. all credit agreements are registered, or negative (as in Belgium), i.e. only failure to pay back leads to

registration. Coupling this with liability for offering credit to consumers indebted to a certain degree would put reasonable onus on industry without freeing the consumer from responsibility for his own actions

Limits to advertising

The increased competition for customers have led to considerable growth in advertising addressed to young consumers, even children. A general ban on advertising addressed to children exists in Sweden (and Greece) and the Swedish government has not hidden its intention to try to promote this at EU level during the Swedish presidency in the first semester of 2001. Given the difference in attitudes to this problem in Member States an alternative to legislation might be a code of good conduct putting limits on the advertising rather than prohibition.

Cost sharing

The need for finance is a routine problem for social work and no less so for debt counselling. More often than not, the public and private funds available are insufficient, and as a result, top quality debt advice cannot be made available across the board.

The credit industry sees credit as the lubricant of the economy — and correctly so: the consumption boom in OECD countries over the last 25 years has been credit financed. However, when you oil a machine there is a risk that some oil may be spilt.; but spilt oil may be slippery, people may fall: If the machine is the economy, people may become over-indebted.

Moreover, creditors are beneficiaries from debt counselling services: The professional skills of these assist the rehabilitation of the over-indebted back into circulation in the economy and thus into the cycle of consumption: E.G., debt advice centres in Germany ensure that 400 million DM is paid back which might otherwise be: lost.

This begs the suggestion of making credit providers co-responsible for «mopping up the spilt oil» by financing at least debt advice and possibly even the insolvency and debt discharge procedures.

The debate on this idea has been going on for some time in Europe; but so far with little if any positive result.

In Germany concrete proposals have been made for a fund covering 15% of the costs of debt advice; this fund would be built through contributions by creditors in the form of levies on creditor claims satisfied through extra-judicial settlements. In Australia reckless lending is, cf. above, punished by fines and these fines are used to finance debt advice. In USA and Great Britain the providers of financial services and mail order businesses provide financial support for money advice.

Arguments of economic logic can be made in favour of the alternative approach, levying a financial contribution from the debtor: debt counselling and debt management represent services that improve the consumer's situation now and, notably, in the future. But obviously, this would only be feasible in very few cases: up front it means adding to the debt burden which makes little sense.

Bringing these considerations together there is an argument for «taxing» the provision of credit. An example of how this could be done is found in the German proposals referred to above: they include a levy of 0.5% on the commission fees of consumer credit agreements. Based on an average level of commission of 2% of the net loan (in Germany at least), the effect of this levy would be to increase the arrangement fee to 2.5%; this, however, only means that the effective interest rate of the credit would increase by about 0.1%.

In the German proposal the sums collected are to be placed in a fund managed by independent welfare associations, consumer organisations, representatives of the creditors and the communes or state authorities. Copying this idea at EU level (building an EU fund) is not feasible for the





simple reason that there are no supra-national debt advice or relief structures. But the proposal could be used as a «benchmark» for co-financing to be copied by other Member States.

2.2. Cure

Despite the opportunities for more «Europeanisation» of credit and debt, the Commission is not convinced that the time has come for a European debt discharge scheme. Given the obligation of the EU to respect the concept of subsidiarity, i.e. only to propose EU regulation if solutions at national or regional level are unlikely to solve the problems, there seems little scope for such a scheme: the differences between national markets for credits and national discharge systems, where existing, are too large to be overcome by a simple over-arching regulation.

However, preparing for such an eventuality or at least ensuring that the knowledge base is in place to allow action if ever — when? — such an idea were to become feasible is perfectly legitimate.

The Commission therefore envisages carrying out an exhaustive analysis of approaches and a review of the pros and cons of these. The Commission would on this basis publish a Recommendation to Member States calling for the setting up of schemes where none exists and, possibly, suggesting «benchmarks» or «best practices» that might encourage the establishment of comparable structures in all Member States, able to co-operate in the context of a more integrated Single Market for consumer credit.