Eurofinas response to the European Commission’s consultation on responsible lending and borrowing in the EU

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SUMMARY OF RESPONSES

As acknowledged by the Commission in its consultation paper, a major step towards a high level of consumer protection across the EU was achieved in the area of consumer credit with the adoption of Directive 2008/48/EC on credit agreements for consumers (the Consumer Credit Directive – CCD)

Eurofinas understands the Commission's objective to carry out a broad reflection at European level on responsible lending and borrowing. Against this background, the Federation is willing to contribute to the Commission's work in a positive and meaningful manner. However, the CCD was adopted a little more than one year ago and is currently being discussed by local regulatory authorities. At this stage, the Federation sees no added-value to further evaluate the CCD provisions.

The transposition of the CCD into Member States legislation will bring substantial modifications to lenders' current business practices. Eurofinas firmly believes that those provisions are adequate in order to guarantee sound lending practices at European level in the field of consumer credit.

At this stage there is no evidence that European consumer credit providers lend irresponsibly and, as regards consumer credit products, no issues which are addressed in the CCD that the new European regulatory framework cannot solve.

Question 1 – Advertising and marketing

- The Federation believes that existing European and National regulatory frameworks are most suitable to prevent consumer credit misleading or unfair advertising or marketing practices and to solve any possible dispute arising in that field.

Question 2 – Risk guidance

- Eurofinas agrees with the Commission that clear information is an essential element in responsible lending and borrowing and that the most significant piece of information disclosure in this context is the pre-contractual information for the credit offer.

- The development of risk guidelines needs to be considered in context. The application of risk guidelines to consumer credit would imply a duty above and beyond the information and explanations which the lenders already have to provide consumers under the CCD.

- Eurofinas strongly opposes the disclosure of risk guidelines in the context of the borrower's discussions with the lender or intermediary.

- Eurofinas would support in principle a description of the general risks associated with borrowing in educational tools that have been set up by financial companies, trade associations or local authorities.

Question 3 – Certification and standardisation of credit products

- Consumer Credit products tend to be of a lower value and less sophisticated in their functionality than other forms of retail products. Within each different product category (e.g. instalment loan, revolving credit) loans share common technical features. These features have been used effectively for many years and reflect consumer demand.

- Eurofinas sees any kind of product certification/standardisation as being contrary to a free market economy.

- Eurofinas believes that any kind of product certification/standardisation is a barrier to product innovation and fluidity in product development which is essential to a dynamic credit market.

Question 4 – Creditworthiness and suitability assessments

- Consumer credit providers always assess the creditworthiness of borrowers. The speed of the overall process has no impact on the quality of the creditworthiness assessment. Intermediaries at the point of sale do not carry out creditworthiness assessments themselves. Intermediaries play no role in the credit granting decision.

- Eurofinas believes that product suitability assessments should not be adapted to the provision of consumer credit.

- Eurofinas believes that if a thorough credit assessment is performed by the consumer credit provider and appropriate information on the credit agreement and the characteristics of the product is provided to the applicant borrower, a further suitability assessment would bring no added value. This is in line with the CCD which emphasizes that the consumer himself should assess the suitability of a credit, after being informed properly by the lender.

Question 5 – Documentation and demonstration of creditworthiness assessment

- A creditworthiness assessment is always documented.

- The adequacy of the creditworthiness assessment can be demonstrated should litigation arise.

- Eurofinas believes that no specific explanations need to be provided to borrowers in the course of the lending transaction with the exception that, where applicable, the lender has checked the consumer’s credit information from a credit bureaux/credit risk agency or public database.

Question 6 – Advice standards

- Eurofinas strongly believes that given the limited risks associated to consumer credit products and the limited average amount borrowed, compulsory advice standards for the provision of consumer credit products would be disproportionate.

- The Federation believes that the lender’s duty to assist consumers by providing adequate explanations (as per the CCD) responds to the need to enable applicant borrowers to make informed decisions as to whether or not they shall enter into a consumer credit agreement.

Question 7 – Responsible borrowing

- Eurofinas agrees with the Commission that responsible borrowing is key.

- Eurofinas believes that financial education and increased EU action to fight fraud is key to encourage responsible borrowing.

Credit intermediaries

Eurofinas welcomes the opportunity to respond to the Commission's questions on credit mediation. Point of Sale (PoS) finance is of particular importance for Eurofinas constituency. Unless explicitly mentioned, the Federation's response focuses on credit mediation at the point of sale.

Question 8 – Definition of credit intermediaries (1)

- Eurofinas sees no reason to differentiate the definition of a credit intermediary of credit products to consumers (i.e. consumer credit and mortgage products) according to whether or not these products are covered by the CCD as long as a distinction between full-time credit intermediaries and persons who offer credit on an incidental basis is maintained.

Question 9 – Definition of credit intermediaries (2)

- Eurofinas believes that, as regards consumer credit, a clear distinction must be made between entities that provide credit mediation to third parties for remuneration as their main activity (e.g. brokers, agents, etc.) and entities that practice credit mediation as an ancillary activity (i.e. dealers and retailers involved in the distribution of credit at the point of sale).

- Retailers and motor dealers have no role in respect of the granting of credit other than collecting information on the consumer on behalf of the lender. Retailers and motor dealers take no part at all in the credit decision. The range of credit products available at the point of sale is limited. Retailers and motor dealers do not act at the consumer's request and consequently, receive no fee from him.

- Given the role dealers play in the distribution of consumer credit at the point of sale, Eurofinas strongly believes that it would be inequitable to subject them to the same requirements as credit brokers.

- As regards other forms of credit mediation, the Federation believes that a distinction should be made between:

    i) intermediaries who are neutral third parties that are not contractually linked with one or several credit providers (untied intermediaries) and,
    ii) intermediaries having a contractual relationship with one or several credit providers who are, in turn, responsible for the activities performed by their tied agents.

Question 10 – Role of credit intermediaries

- Eurofinas strongly believes that current European and National regulatory frameworks, along with credit providers' strict control and supervision of retailers and motor dealers involved in the distribution of credit at the point of sale, effectively prevent cases of misconduct or mis-selling.

Question 11 – Framework for credit intermediaries

- As mentioned in Europe Economics study on *credit intermediaries in the Internal Market*, there is currently limited explicit statutory regulation of PoS intermediaries across Europe. Eurofinas believes that far from creating a legal gap it reflects a common approach according to which retailers and motor dealers involved in the distribution of credit at the point of sale are considered to act under the full responsibility of credit providers. This is because all regulatory provisions to which consumer credit providers are subjected are necessarily reflected at the point of sale.

- The idea that PoS finance may facilitate the provision of consumer credit cross-border is theoretical. In practice, most credit providers do cross-border business by creating local subsidiaries or branches in other European markets. The role of PoS finance in the development of direct cross-border credit has, therefore, still to be demonstrated. Because PoS finance is intrinsically a local activity, it would not benefit from a single European passporting regime.

Question 12 – Information disclosure on credit intermediaries

- Retailers and motor dealers do not receive any payments from borrowers for the provision of credit at the point of sale.

- As regards potential conflicts of interest with regard to commission structures, Europe Economics concluded that in comparison with other forms of credit mediation, potential conflict of interest due to PoS intermediaries' remuneration schemes was considered as absent.

- Eurofinas agrees with Europe Economics' findings and believes that the risk of potential conflict of interest due to PoS intermediaries' remuneration schemes is extremely limited.

Question 13 & 14 – Registration, licensing and supervision of credit intermediaries

- Eurofinas strongly believes that prudential and supervision requirements for retailers and motor dealers involved in the distribution of credit at the point of sale are unnecessary and that applying the same requirements to retailers and motor dealers as for credit brokers would be disproportionate and inequitable given their limited role in the distribution of consumer credit at the point of sale.

Question 15 – Complaints and redress

- Given the role retailers and motor dealers play in the distribution of consumer credit at the point of sale**,** any disputes arising from the distribution of credit at the point of sale will involve the credit provider and therefore benefit from the ADR schemes in place. The Federation therefore believe that there is no need to promote further out-of-court mechanisms for PoS finance.

- Other forms of credit mediation (i.e. brokers and the like), are already covered by ADR mechanisms in several markets. Eurofinas therefore recommends that the Commission carries out a preliminary assessment in order to identify in which Member States such procedures are already in place (whether or not via regulation).

ABOUT EUROFINAS

Eurofinas, the European Federation of Finance House Associations, is the voice of the specialised consumer credit industry at European level. It currently represents 17 Member Associations, in turn bringing together more than 1,000 finance houses, captive companies, specialised and universal banks. Together, these consumer credit providers financed over 400 billion euros worth of new loans during 2008, with outstandings reaching 745 billion euros at the end of the year. Companies represented through Eurofinas employ some 90 000 individuals.

Consumer credit providers may be of several natures and our members' members can be grouped into the categories below. Around 90% of the companies represented through Eurofinas are specialised lenders, falling into the first three categories:

- Finance houses: specialised consumer credit providers without a banking licence;

- Captive companies: parent companies of these companies are manufacturers (e.g. car manufacturers). Captives may or may not have a banking licence;

- Specialised banks : institutions with a banking licence but an activity focused on consumer credit or/and mortgage lending; and

- Universal banks: banks providing all kinds of products retail, corporate, etc., including consumer credit.

INTRODUCTORY OBSERVATIONS

Eurofinas, the voice of specialised consumer credit providers in Europe welcomes the opportunity to respond to the European Commission's public consultation on responsible lending and borrowing in the EU[1].

As acknowledged by the Commission in its consultation paper, a major step towards a high level of consumer protection across the EU was achieved in the area of consumer credit with the adoption of Directive 2008/48/EC on credit agreements for consumers (the Consumer Credit Directive – CCD).

Consumer Credit Directive

The Consumer Credit Directive was adopted on 23 April 2008 after more than five years of intense discussions amongst all interested parties. This new European regulation covers all aspects of the consumer credit lending transaction:

- Standard information to be included in consumer credit advertising
- Pre-contractual information to be provided to applicant borrowers via the Standard European Consumer Credit Information Sheet (SECCI)
- Assessment of applicant borrowers' creditworthiness
- Contractual information to be included in all credit agreements
- Specific information related to the borrowing rate to be provided to consumers
- Calculation of the annual percentage rate of charge (APRC)
- Transparency measures for intermediaries involved in the provision of consumer credit agreements (i.e. disclosure of extent of power and fees payable by the consumer to the intermediary)
- Where necessary, additional assistance to be provided to the applicant borrower in order to decide which credit agreement is the most suitable for his needs and financial situation
- Borrowers right of withdrawal from the credit agreement
- Borrowers right to discharge, fully or partially and at any time his obligations under a credit agreement
- Lenders liability for credit agreements linked to the purchase of goods or services
- Out-of-court dispute resolution schemes for the settlement of consumer disputes concerning credit agreements

The transposition of the CCD into Member States legislation will bring substantial modifications to lenders' current business practices. As a consequence, lenders will have to adapt their processes, advertising and marketing materials, information documents, staff training and IT systems to the new legal framework. Needless to mention that such a process takes time and is resource-intensive.

[1] Unless explicitly mentioned in the document in hand, Eurofinas response focuses on the provision of consumer credit. As regards credit mediation, unless explicitly mentioned in the document in hand, Eurofinas response focuses on credit distributed at the point of sale (PoS finance).

Member States should adopt the provisions necessary to comply with the CCD by 11 June 2010. **Eurofinas firmly believes that those provisions are adequate in order to guarantee sound lending practices at European level in the field of consumer credit.**

In light of the elements mentioned above, the Federation questions the Commission's statement in its consultation paper that the effects of the CCD provisions are unclear.

The new European regulatory framework is designed to *i)* ensure that all European consumers enjoy a high and equivalent level of protection and *ii)* facilitate the emergence of a well-functioning internal market in consumer credit. This new framework will inevitably impact upon business practice and consumers legal rights. In accordance with Article 27 of the CCD, Eurofinas understands that on the basis of a regular monitoring and thorough assessment, modifications may be proposed.

These modifications can however only be meaningful once the provisions will have been adequately transposed by local regulators and implemented by lenders in all European markets.

Eurofinas understands the Commission's objective to carry out a broad reflection at European level on responsible lending and borrowing. Against this background, the Federation is **willing to contribute to the Commission's work in a positive and meaningful manner**. However, the CCD was adopted a little more than one year ago and is currently being discussed by local regulatory authorities. **At this stage, the Federation sees no added-value to further evaluate the CCD provisions.**

Eurofinas agrees with the Commission that it is in lenders' interests to lend responsibly.

However the consultation paper mentions that "as evidence from the current economic crisis has shown, there is still significant room for irresponsible lending and borrowing to take place" and that "certain issues which were deliberately not or partially harmonized in the Directive [the CCD] may need to be worked on in the light of the financial crisis".

The Federation wishes to clarify the context of this discussion.

From the Commission's recent Communication for the Spring European Council – *Driving European recovery* – Eurofinas understands that the recent financial crisis has led the Commission to propose a reform programme in order to deliver responsible and reliable financial markets for the future. In this respect, the Federation supports in principle the European work on supervisory structure.

However, the issue of retail responsible lending in Europe should be clearly distinguished from the present financial crisis which was generated by US subprime lending. The current financial turbulences did not originate via the provision of retail credit in Europe. Any links between the worldwide financial crisis and the provision of retail credit in Europe would not only be wrong but absolutely misleading.

When considering the results of the consultation and its possible next steps, Eurofinas believes that the Commission should perform an in-depth analysis of the issues (if any) that arise due to the absence of an EU level initiative in the field of responsible lending and borrowing. When conducting this analysis, it is crucial that the Commission takes account of consumer protection rules that will soon apply to the provision of consumer credit and initiatives that have recently been adopted or are currently being discussed at national level.

The Federation firmly believes that responsible lending is a priority for consumer credit lenders. One of the overriding requirements of profitable and successful lending is that lenders provide finance to borrowers who can repay the credit with interest. **It does not make economic sense for lenders to deliberately lend irresponsibly.**

At this stage there is no evidence that European consumer credit providers lend irresponsibly and, as regards consumer credit products, no issues which are addressed in the CCD that the new European regulatory framework cannot solve.

Significantly, this consultation is set against the backdrop of the most difficult conditions for lenders for a considerable time.

In 2008, the average consumer credit loan was of 6018 Euros[2]. This represents a decrease of 6.5 % compared to the year 2007. In 2008, the total of new consumer credit granted reached 268,2 billion Euros and 40639 million new contracts[3]. This respectively represents a decrease of 8.3% and 1.5% compared to the year 2007. Information from Eurofinas member associations shows that this trend has worsened in the first months of 2009.

Consumer lending is vital to enhance personal consumption which is a key driver for economic recovery. Eurofinas therefore believes that when conducting its analysis it is crucial that the Commission bears this situation in mind and seriously considers that potential new regulation will inevitably further affect the industry.

In addition, retail lending comprises many distinct products and distributional channels. It is therefore paramount that these differences are reflected in the Commission's analysis.

[2] Based on Eurofinas statistics for the year 2008 and including personal loans, credit at the point of sale and vehicle finance (new and used cars for private use and other vehicles (motorcycles, caravans etc.)).
[3] Based on Eurofinas statistics for the year 2008 and including all consumer credit for personal consumption and vehicle finance (new and used cars for private use and other vehicles (motorcycles, caravans etc.)).

PRACTICES PRIOR TO THE LENDING TRANSACTION

Question 1: *Do you have evidence of misleading or unfair advertising or marketing practices with regard to mortgage and consumer credit?*

Eurofinas has no evidence of misleading or unfair advertising or marketing practices with regard to consumer credit.

The Federation believes that existing European and National regulatory frameworks are most suitable to prevent misleading or unfair advertising or marketing practices **and** to solve any possible dispute arising in that field.

Consumer Credit Advertising

According to Article 4 of the CCD, any advertising concerning credit agreements which indicates an interest rate or any figures relating to the cost of the credit to the consumer shall include a set of standard information as follows:

- the borrowing rate (fixed or variable or both) together with particulars of any charges included in the total cost of the credit to the consumer
- the total amount of credit
- the annual percentage rate of charge (APRC)
- if applicable, the duration of the credit agreement
- in the case of a credit in the form of deferred payment for a specific good or service, the cash price and the amount of any advance payment
- if applicable, the total amount payable by the consumer and the amount of the instalments

This clearly means that all advertising and marketing materials for consumer credit will provide consumers with information on the <u>total cost</u> of the credit, its <u>duration</u>, the <u>amount of instalments</u> and <u>possible amount of advance payment</u> in the case of a deferred payment.

It should also be specified that where the conclusion of an ancillary contract to the credit agreement is compulsory in order to obtain the credit or to obtain it on the terms and conditions marketed and the cost of that service cannot be determined in advance, the obligation to enter in that contract will be provided in the advertising material. **Eurofinas strongly believes that such binding provision on lenders is appropriate to prevent any misleading conduct.**

In addition, the Federation wishes to specify that under the CCD, not only standard information needs to be provided but it should be mentioned in <u>clear, concise and prominent way by means of a representative example</u>.

Standard information has therefore to be comprehendible for consumers and be provided by means of an example. The latter will help potential borrowers to immediately visualize the conditions and the concrete impact of the advertised credit offer. Eurofinas believes that these elements are adapted to the consumer credit advertising and complement existing European misleading and comparative advertising regulation.

Consumer Credit advertising is also covered by the Unfair Commercial Practices Directive which prohibits unfair commercial and misleading advertising practices in business to consumer transactions.

In this context Eurofinas recalls that a practice should be regarded as misleading if it contains false information and is therefore untruthful or deceives or is likely to deceive the average consumer even if the information is factually correct. A practice should be regarded as misleading if it omits material information that the average consumer needs to take an informed transactional decision or causes or is likely to cause the average consumer to take a transactional decision that he would not have taken otherwise.

The Federation believes that the combination of (1) the prohibition of misleading actions and omissions (2) the ability for Member States to impose more restrictive requirements for financial services under the Unfair Commercial Practices Directive and (3) the compulsory standard information to be included in advertising/marketing materials under the CCD form an exhaustive regulatory framework which prevents consumer credit providers from introducing unfair or misleading advertising.

In this context, the Federation wishes to recall the importance of a uniform transposition and implementation of the CCD.

Were any lender to introduce such type of advertising, then action could be taken under the Unfair Commercial Practice Directive. This might include the intervention of the competent administrative authority to decide on launching a complaint or to initiate proceedings. In addition, where any standard information is omitted from a consumer credit advertisement, consumers can take legal action against the lender and/or address its claim to an out-of-court dispute resolution body (whose existence is compulsory under the CCD).

Question 2: *What are your views on the development of risk guidelines?*

Eurofinas agrees with the Commission that clear information is an essential element in responsible lending and borrowing and that the most significant piece of information disclosure in this context is the pre-contractual information for the credit offer.

Comprehendible and concise pre-contractual information is key for an applicant borrower to assess whether he wishes to enter into a contractual relationship with the lender.

As mentioned in the consultation paper, according to article 5 of the CCD, the lender and, where applicable, the credit intermediary should provide the consumer with the information needed to compare different offers in order to take an informed decision on whether to conclude a credit agreement. This information will be provided by means of the Standard European Consumer Credit Information (SECCI) form.

The SECCI provides the applicant borrower with an exhaustive list of information on the credit agreement. In addition to the SECCI, credit providers and, where applicable, credit intermediaries should provide adequate explanations to the consumer, in order to place the consumer in a position enabling him to assess whether the proposed credit agreement is adapted to his needs and to his financial situation, where appropriate by explaining the pre-contractual information, the essential characteristics of the products proposed and the specific effects it may have on the consumer, including the consequences of default in payment by the consumer.

The development of risk guidelines needs to be considered in context. First of all, the risk involved in consumer credit lending is lower than for other forms of retail lending or financial products. Risks are rather related to unexpected changes in consumers' personal situation (e.g. job loss, illness etc.).

As mentioned previously, in 2008 the average consumer loan was of 6018 Euros[4]. There is clearly an important difference between concluding a credit agreement for the purchase of a property and for the purchase of household appliances.

The Federation believes that consumer credit products are easily understood by the average consumer as long as proper information (as per the CCD) is provided to him. They tend to be of a lower value and less sophisticated in their functionality than other forms of retail products.

That said, the notion of financial risk is extremely variable depending on the social group to which a consumer belongs. **Therefore there cannot be any 'one size fits all' solution**. Indeed, should a consumer be unable to understand the implications of concluding a credit agreement despite *i)* the pre-contractual information form provided to him, *ii)* the lender's explanations of the essential characteristics of the product proposed and *iii)* the specific effects it may have on him including the consequences of default in payment, the Federation believes that there is very little chance that this consumer will actually understand any risk warnings.

[4] Based on Eurofinas statistics for the year 2008 and including personal loans, credit at the point of sale and vehicle finance (new and used cars for private use and other vehicles (motorcycles, caravans etc.)).

In that case, the issue goes far beyond responsible lending and is about the most vulnerable parts of the population grasping the most basic economic concepts such as budgeting, savings or planning ahead.

The application of risk guidelines to consumer credit would imply a duty above and beyond the information and explanations which the lenders already have to provide consumers under the CCD.

Finally the Federation is concerned about potential detrimental effects of risk guidelines on consumers' access to credit. Eurofinas believes that consumer protection should not inhibit the supply of sustainable credit, particularly to those most in need.

Eurofinas therefore strongly opposes the disclosure of risk guidelines in the context of the borrower's discussions with the lender or intermediary. Not only would such information be redundant in light of the explanations which already have to be provided by the lender but it would create an unmanageable information overload both for the consumer and the lender. Further, such disclosure would be completely disproportionate to the limited risks involved and the average consumer's understanding of consumer credit.

Eurofinas believes that any problems identified in specific consumer credit markets, should be resolved by the CCD's provisions.

Eurofinas understands the Commission's concern to raise consumer awareness of the financial risks inherent to financial services, in particular when considering the conclusion of a credit agreement. Eurofinas would therefore support in principle a description of the general risks associated with borrowing in educational tools that have been set up by financial companies, trade associations or local authorities.

BUSINESS PRACTICES IN THE CONTEXT OF LENDING TRANSACTIONS

Question 3: *In your view, are there certain categories of credit products that are inherently unsuitable for sale to retail borrowers? Would you welcome a set of standardised or certified credit products to be offered to consumers?*

As a preliminary remark, it should be stressed that consumer credit products are less sophisticated in their functionality than other forms of banking and financial products. Within each different product category (e.g. instalment loan, revolving credit) loans share common technical features[5]. These features have been used effectively for many years and reflect consumer demand.

Consumer credit providers differentiate themselves by:

- identifying and targeting specific market segments
- developing or optimizing cumulative or alternative use of direct and indirect distribution channels
- developing or adapting consumer credit products and services to the latest technological changes
- promoting marketing campaigns and co-branding consumer credit products

Eurofinas sees any kind of product certification/standardisation as being contrary to a free market economy.

Eurofinas believes that any kind of product certification/standardisation is a barrier to product innovation and fluidity in product development which is essential to a dynamic credit market. Consumer credit markets are some of the most dynamic markets in financial services. The understanding of and adaptation to consumers' needs and wants is at the heart of innovation by specialised lenders.

Consumers needs and wants vary from one country to another. The advantages and disadvantages of different products therefore depend on the specific circumstances that prevail when entering into an agreement. The debates which took place during the drafting of the Consumer Credit Directive on the definition of "consumer credit" show how the promotion of common standardised elements is extremely difficult if not impossible.

In parallel, the Federation wishes to emphasize that lenders do not grant loans as a one-off business proposition, but are looking forward to a long-term relationship with their customers. The long-term quality of lenders' portfolio is vital. Before launching a credit product lenders therefore conduct numerous suitability assessments. Standardisation would create unnecessary competitive distortions and decrease the availability of consumer credit products.

Eurofinas believes that promoting good practice in itself is laudable. However, regulating products through standards would bring no added value. Instead, having robust principles of transparency, information and competence (i.e. having a clear governance framework) would be more beneficial in terms of consumer protection.

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[5] Another example is that of international credit cards which share common technical features in turn allowing their large acceptance.

Question 4: *Do you consider that mortgage lenders and credit intermediaries should always perform creditworthiness and/or suitability assessments before granting consumer and mortgage loans? For mortgage credit, what are your views on the criteria to be used in assessing suitability such as loan-to-income ratios or loan-to-value ratios?*

As a preliminary remark Eurofinas would like to clarify the elements mentioned in the Commission's consultation paper.

Creditworthiness assessment

When deciding on whether or not to grant a loan or a credit facility to a consumer, a lender has to assess the creditworthiness of its potential borrower, i.e. he must examine the individual's ability to meet his or her financial commitments to repay the loan. **Creditworthiness assessment therefore consists of evaluating the applicant borrower's solvency**.

This assessment is performed by using different sources of information such as:

- The loan application form or other information supplied by the potential borrower to the lender (income, family status, length of employment, number of loan applications etc.);
- Experience of business relations with the potential borrower to date (credit history, including current and past credit commitments);
- Credit bureaux/credit risk agencies whose role is to provide credit information on consumers; and,
- Depending on the country, public sources including bad debtor lists, court judgements or bankruptcies in the applicant's name.

Credit scoring systems

When considering applications for borrowing, most lenders throughout the developed economies use computer-aided schemes known as credit scoring systems. These systems have been judged by regulators in many countries as being beneficial to the consumer, the lender and to the economy. The World Bank in particular supports their use.

To evaluate creditworthiness as objectively and accurately as possible, credit scoring systems carefully and precisely gather and use information about the customer from a variety of sources.

The component parts of each system vary for each lender based on its own earlier experience gleaned from customers who pay well or badly. The end result is a scorecard containing a series of factors with associated numeric values. Its development and validation uses established statistical principles In operation, the system gives points for each piece of relevant information and adds these up to produce a score. If the customer's score reaches a certain level, the lender will generally accept the application. If the score does not reach this level, the application may not be accepted without good reason.

Additional rules, reflecting the lender's commercial experience and needs, may also be used when deciding whether to lend together with any relevant or up to date information. The score is a very important factor when determining whether or not to grant a loan, but it may not be the only one. Consequently the final decision is taken by considering all the information available.

Every credit or loan application involves a certain level of risk to the lender, irrespective of "quality" of the potential borrower. Credit scoring allows the lender to work out a statistically reliable estimate of the risk level for each applicant. If the level of risk is deemed to be too high, the lender will not accept such an application. This does not mean that any applicant turned down is a bad payer. It simply means that, based on the available information and the experience with similar applications the lender is not prepared to take the risk of providing that credit.

Lenders are not obliged to accept any application. Each lender applies its own policies and has different scoring systems. Therefore, applications may be assessed differently by different lenders with the result that one lender may accept an application while another lender may not. **Deciding upon acceptable levels of risk is and should remain a business decision**.

Suitability assessment

The suitability assessment is a totally different mechanism which consists in evaluating whether a specific product is suitable to a specific customer. As mentioned in the Markets in Financial Instruments Directive, it consists of obtaining necessary information on the potential client's financial situation, knowledge and experience and objectives in order to assess whether a product/service is suitable for him/her.

The creditworthiness assessment consists in evaluating whether the potential borrower has the ability to repay a loan. The suitability assessment consists in evaluating which product or service suits best to the potential borrower.

The consultation paper states that there are a number of disincentives to carry out creditworthiness assessment. It should however be stressed that:

- Consumer credit **providers <u>always</u> assess the creditworthiness of borrowers.**
- **The speed of the overall process has no impact on the quality of the creditworthiness assessment**.
- **Intermediaries** at the point of sale **do not carry out creditworthiness assessments themselves**. All the information collected on the applicant borrower by the intermediary is checked by the lender before any credit decision is made, should it be instantly via online application or, later on, after the intermediary has communicated all relevant data to the lender.
- **The ability to repay and/or the credit limit are never driven by the intermediary but by the lender (through IT scoreboards). <u>Intermediaries play no role in the credit granting decision</u>.**

- Intermediaries at the point of sale cannot interfere with lender's creditworthiness assessment process (i.e. the software or other systems) and only have access to a result in the form of a particular credit decision.

[Please see further explanations on Point of Sale finance processes in Eurofinas response to questions related to credit intermediaries]

Eurofinas believes that product suitability assessments should not be adapted to the provision of consumer credit. This is because:

- Consumer credit products are easily comparable because information and many other requirements are standardised. This will become even more so with the provision of the SECCI under the CCD;

- Consumer credit products tend to be less sophisticated in their functionality than other forms of retail products.The introduction of a compulsory suitability assessment similar to the one performed by investment firms when providing investment services to their clients (as required by the Markets in Financial Instruments Directive) would be absolutely disproportionate.

- The amount borrowed is usually limited in comparison to first charge mortgages. For example, in 2008 the average loan granted at the point of sale was of 1589 Euros[6].

- A substantial proportion of consumer credit products is distributed at the point of sale, where the range of available products is limited. Products are designed to respond to consumers specific needs. Depending on the selected goods and services, suitable finance solutions will be available to consumers. Above all, the retailers or car dealers involved in the distribution of credit at the point of sale are not in a position to assess the suitability of products.

- As previously mentioned, the majority of debt situations occur when borrowers experience payment problems due to unpredictable changes in circumstances after the loan was taken out such as unemployment, relationship breakdown or illness.

Eurofinas believes that if a thorough credit assessment is performed by the consumer credit provider and appropriate information on the credit agreement and the characteristics of the product is provided to the applicant borrower, a further suitability assessment would bring no added value. This is in line with the CCD which emphasizes that the consumer himself should assess the suitability of a credit, after being informed properly by the lender.

In parallel Eurofinas would like to draw the Commission's attention to the potential risks of product suitability. This could include driving the market to monoline products and making the credit granting process less flexible. A suitability assessment implies subjective elements which are part of an advice mechanism and which, in the opinion of the Federation, is not adaptable to the provision of consumer credit products.

[6] Based on Eurofinas statistics for the year 2008 and include consumer credit at the point of sale for the financing of consumer goods (electronic and household appliances).

Question 5: *How should the lender or credit intermediary demonstrate or document the adequacy of the credit worthiness and suitability assessment?*

Consumer credit providers always assess the creditworthiness of applicant borrowers. At the point of sale, intermediaries never carry out creditworthiness assessments themselves.

As previously mentioned, the creditworthiness assessment of a potential borrower is performed by using different sources of information such as the information provided by the borrower to the lender, credit information held on consumers etc.

Using sophisticated credit scoring techniques, the lender uses this information to assess whether the applicant borrower is able to meet his or her financial commitments to repay the loan in accordance with the lender's risk policy.

A creditworthiness assessment is therefore always documented (i.e. based on information obtained from the loan application, consultation of credit bureaux/credit risk agencies, consultation of public data sources and/or past business records with the borrower).

The adequacy of the creditworthiness assessment can be demonstrated should litigation arise.

The Federation believes that no specific explanations need to be provided to borrowers in the course of the lending transaction with the exception that, where applicable, the lender has checked the consumer's credit information from a credit bureaux/credit risk agency or public database.

Question 6: *Do you think that these advice standards would be appropriate in an EU context? Are there others that should be considered? What would be the most appropriate means to introduce and enforce the application of advice standards?*

According to article 5 of the CCD, the lender and, where applicable, the credit intermediary should provide the consumer with the information needed to compare different offers in order to take an informed decision on whether to conclude a credit agreement. This information will be provided by means of the SECCI form.

The SECCI provides the applicant borrower with an exhaustive list of information on the credit agreement. In addition to the SECCI, credit providers and, where applicable, credit intermediaries should provide adequate explanations to the consumer, in order to place the consumer in a position enabling him to assess whether the proposed credit agreement is adapted to his needs and to his financial situation, where appropriate by explaining the pre-contractual information, the essential characteristics of the products proposed and the specific effects it may have on the consumer, including the consequences of default in payment by the consumer.

Eurofinas strongly believes that given the limited risks associated to consumer credit products and the limited average amount borrowed, compulsory advice standards for the provision of consumer credit products would be disproportionate.

The Federation believes that the lender's duty to assist consumers by providing adequate explanations responds to the need to enable applicant borrowers to make informed decisions as to whether or not they shall enter into a consumer credit agreement.

It is worth highlighting that many different distribution channels are used by lenders to distribute consumer credit products. It is not possible to provide personalised advice to borrowers for credit distributed at the point of sale or via the internet. This is because neither retailers nor motor dealers are in a position to advice applicant borrowers or because the entire lending transaction is performed via the lender's website.

At this stage, Eurofinas would therefore recommend the Commission awaits the implementation of the CCD before assessing whether further action is needed.

When considering the results of the consultation and its possible next steps, Eurofinas believes that the Commission should perform an in-depth analysis of the issues (if any) that arise due to the absence of EU advice standards for consumer credit products.

Finally, Eurofinas is concerned about the potential level of claims which, if successful could deem credit providers contracts unenforceable on the basis of technical or unintended breaches. The Commission is encouraged to consider the consequences on the European credit market if penalties levied on lenders for lending which is later deemed to be irresponsible or unsuitable would similarly lead to contracts being deemed unenforceable.

The Commission should be aware that any increase in legal and administrative costs will inevitably lead to an increase of cost of credit.

RESPONSIBLE BORROWING

Question 7: *Apart from a focus on financial education, are there any measures that could be taken to encourage responsible borrowing?*

Eurofinas agrees with the Commission that responsible borrowing is key.

The Federation believes that irresponsible borrowing cover two different types of situations:

- insufficiently-educated consumers who may not fully understand all the consequences of entering into a credit agreement
- consumers acting dishonestly and who deliberately provide wrong/misleading information to lenders

Eurofinas agrees that financial education is crucial to promote responsible borrowing. Against this background, Eurofinas supports educational programmes – undertaken by trade associations, consumer representatives and firms – which aim to increase consumers' financial literacy.

Additionally, **Eurofinas believes that increased EU action to fight fraud is key to encourage responsible borrowing.**

Of particular concern is that little data is currently available on how to identify fraudsters and combat fraud/. Any data that does exist is not set out in a homogenous and comparable form. Fraud causes substantial financial damage for lenders, who must dedicate expensive resources to identify and prevent fraudulent acts. Lenders incur tangible losses due to fraud. It also has reputational consequences.

In times of economic hardship, lenders have found that the number of fraud cases, both actual and attempted, rise[7].

Fraudulent activity results in consumer detriment. Amongst others, fraud can:

- lead to higher interest rates for all consumers, as lenders seek to recover losses incurred as a result of fraudulent activity; and
- have a negative impact upon the credit history of a borrower, if loans are fraudulently taken out in the borrower's name.

In line with the conclusions of the Expert Group on Credit Histories (EGCH), the Federation notes in parallel that facilitated access to, and exchange of, credit data also encourages responsible borrowing by consumers[8].If consumers who borrow cross-border realise that lenders have the ability to access foreign credit databases, the said consumers may begin to pay more attention to their own credit histories.

This could lead to such consumers having a clearer picture of their own financial situation, in turn helping to increase responsible borrowing and to reduce levels of consumer indebtedness.

[7] The rise of actual fraud can be limited by anti-fraud initiatives some of which have been implemented by Eurofinas members (e.g. AVCIS scheme in which the UK Finance & Leasing Association is involved).
[8] See EGCH Report, Section 3.2.2, p. 14

CREDIT INTERMEDIARIES

Introductory remarks

Eurofinas welcomes the opportunity to respond to the Commission's questions on credit mediation. Point of Sale (PoS) finance is of particular importance for Eurofinas constituency. Unless explicitly mentioned, **the Federation's response will therefore focus on credit mediation at the point of sale**.

PoS Finance

PoS finance is an indirect distribution channel through which lenders distribute their products at the point of sale. In this particular context, it should be remembered that credit intermediaries are retailers or motor dealers practising credit mediation as an ancillary activity. Retailers and motor dealers act on behalf of credit providers, receive no fee from consumers and are not entitled to advise them. There is no general rule in terms of agreement exclusivity: retailers and motor dealers can have exclusive or non-exclusive partnerships with lenders.

The financing of goods and services at the point of sale may be performed through different types of credit products:

First, goods and services can be financed through **linked credit agreements**. As defined in the CCD, a linked credit agreement means a credit agreement where the credit serves exclusively to finance an agreement for the supply of a specific good or service.

Distribution of credit at the point of sale may also be performed through **store or credit cards**.

The percentage of Eurofinas new consumer credits distributed via the point of sale was 43% in 2003 and 37 % in 2007.

Looking at three large markets, Eurofinas 2007 statistics show that 32% of total new credits (to consumers and businesses alike) were granted through indirect channels in the UK by Eurofinas members, 64% in Italy and 70% in Germany. **PoS finance represents between 86% (UK) and 92% (DE) of total new consumer credits granted through indirect channels by Eurofinas members**. **Between 62% (IT) and 76% (DE) of credit granted at the point of sale was linked to the purchase of a car**.

An important number of market players are active in the financing of goods and services at the point of sale. These are **specialised lenders**, the principal activity of which is to carry out consumer lending. A number of these institutions are captive finance companies of manufacturers, daughter companies of manufacturers.

Eurofinas believes that a clear distinction must be made between entities that provide credit mediation to third parties for remuneration as their main activity (e.g. brokers, agents, etc.) **and entities that practice credit mediation as an ancillary activity** (i.e. dealers and retailers involved in the distribution of credit at the point of sale).

EC Question 8: *Do you consider that the scope of the definition of Credit Intermediary as set out in the Consumer Credit Directive could also be applied to the mediation of credit not covered by that directive? Would it be appropriate to differentiate between full-time credit intermediaries and persons who offer credit intermediation on an incidental basis?*

Eurofinas sees no reason to differentiate the definition of a credit intermediary of credit products to consumers (i.e. consumer credit and mortgage products) according to whether or not these products are covered by the CCD as long as a distinction between full-time credit intermediaries and persons who offer credit on an incidental basis is maintained.

EC Question 9: *Do you think policymakers should make distinctions between credit intermediaries in terms of the products they sell (mortgage, consumer credit, point of sale credit)? Should credit intermediaries be treated differently in terms of the status of their relationship with lenders (tied versus untied intermediaries)? Please explain your answer.*

Eurofinas believes that, as regards consumer credit, a clear distinction must be made between entities that provide credit mediation to third parties for remuneration as their main activity (e.g. brokers, agents, etc.) and entities that practice credit mediation as an ancillary activity (i.e. dealers and retailers involved in the distribution of credit at the point of sale).

Retailers and motor dealers have no role in respect of the granting of credit other than collecting information on the consumer on behalf of the lender. Retailers and motor dealers take no part at all in the credit decision. The range of credit products available at the point of sale is limited. Retailers and motor dealers do not act at the consumer's request and consequently, receive no fee from him.

The developments below provide detailed explanations on the functioning of credit mediation at the point of sale.

Summary

I. WHAT IS POS FINANCE?

i) PoS finance contribution to global consumption
ii) PoS finance importance and growth
iii) Typical products offered at PoS
iv) Typical Goods and Services financed at PoS

II. HOW DOES POS FINANCE WORK?

i) Lender's selection of credit intermediaries
ii) Lender's monitoring of credit intermediaries
iii) Lender's assistance and support to credit intermediaries
iv) Lender's training of credit intermediaries

I. WHAT IS POS FINANCE?

PoS finance is an indirect distribution channel through which lenders distribute their products at the point of sale. Credit granted at the point of sale allows consumers to purchase goods and services, thereby contributing to overall consumption expenditure.

i) PoS finance contribution to global consumption

Total new consumer credit granted at the point of sale (2008)[9]	
	€Mil
BE	2,611
CZ	1,230
DE	17,238
ES	13,348
FI	1,115
FR	11,898
UK	19,760
IT	23,400
NL	1,301
NO	2,152
PT	2,192
SE	2,225
Total	**98,470**

In 2008, more than €98.470 billion of goods, services and consumer vehicles were financed at the point of sale by Eurofinas members (based on a sample of 12 member countries and excluding goods and services financed via credit/store cards).

This figure underlines the importance of point of sale finance for consumers and retailers to acquire and distribute goods and services respectively.

PoS finance therefore plays a crucial role in supporting global consumption.

[9] Based on Eurofinas statistics for the year 2008.

Car penetration rates in 2006[10]

Car Penetration in 2006	
Country	Penetration Rate*
BE	40.99%
DE	26.11%
ES	73.72%
FI	31.35%
IT	71.25%
NL	17.75%
SE	32.91%
UK	47.50%
Eurofinas	**60.91%**
*Penetration rate is calculated by taking the number of new passenger car finance contracts for private use (Eurofinas figures) and dividing by the number of new passenger car registrations (ACEA figures)	

In 2006, Eurofinas members financed at the point of sale 60.9% of new passenger cars registered for private use (based on a sample of 8 member countries).

This figure shows the importance of point of sale finance for consumers, motor dealers and car manufacturers alike to acquire and distribute passenger cars for private use.

The Italian, Spanish, UK & German markets financed the greatest proportion of new passenger cars amongst Eurofinas members. Respectively, they financed 71.3%, 73.7%, 47.5% & 26.1% of the new passenger cars that were registered in their respective market.

In 2006, more than 60 % of new passenger cars for private use were financed at the PoS.

[10] Car penetration rates provided in the document in hand are based on ACEA's latest available statistics.

ii) PoS finance importance and growth

The distribution of credit at the point of sale plays a crucial role for:

i) **Motor dealers** for which PoS finance is an indispensable tool for the sale of vehicles;

ii) **Retailers** for which PoS finance is a commercial tool and a vital need for `big ticket´ items (goods sold for more than 500 Euro);

iii) **Consumers** for which finance at the point of sale is particularly crucial when considering the purchase of a vehicle or big pieces of white or brown goods (Refrigerator, Televisions, Computers etc.)[11]; and

iv) **Manufacturers** as a key tool to distribute their production.

POS Finance in 2008[12]

	Consumer Vehicle Finance		Credit granted at Point of Sale for Goods & Services	
Country	New credit granted (mil€)	% change to previous year	New credit granted (mil€)	% change to previous year
BE	2,379	3.4%	232	5.5%
CZ	498	31.1%	732	18.9%
DE	14,829	-1.4%	2,409	7.9%
ES	8,420	-31.1%	4,928	-6.5%
FI	1,115	-24.7%	na	na
FR	7,623	-0.9%	4,275	8.1%
UK	15,626	-19.2%	4,134	-9.6%
IT	18,392	-13.6%	5,008	-10.2%
NL	1,136	7.5%	165	-29.2%
NO	2,152	-9.6%	na	na
PT	1,728	-6.3%	464	9.2%
SE	1,767	-0.7%	458	-5.2%
Eurofinas	**75,665**	**-12.8%**	**22,805**	**-3.3%**

In 2008, more than €98.470 billion of goods, services and new passenger vehicles were financed at the point of sale by Eurofinas members.

[11] White goods: large household appliances, as ovens and refrigerators.
Brown goods: audio/visual and consumer electronic products such as televisions, radios, and stereo sets.
[12] Based on Eurofinas statistics for the year 2008.

When acquiring a good or a service, consumers may have several purchasing options. Consumers may pay directly for the said good or service or may request a finance solution at the point of sale.

Depending on the selected goods and services or nature of the point of sale, several types of finance solution such as a linked credit or a store/credit card may be available to consumers.

As a general observation, it would be wrong to suggest that consumers take out credit at the point of sale because they cannot obtain credit with traditional banks. Customers' profile is extremely diverse, ranging from lower to higher social categories. There are numerous benefits to PoS finance. These include convenience and a deal that can be adapted to a consumer's budget.

iii) Typical products offered at PoS

Linked credit

The financing of goods and services may be performed through linked credit agreements.

As defined in the CCD, a linked credit agreement means a credit agreement where the credit serves exclusively to finance an agreement for the supply of a specific good or service. Those two agreements form, from an objective point of view, a commercial unit, which implies pragmatic and rationale behaviour by the consumer.

Point of sale finance (i.e. via linked credit agreements) is common in the motor and retail (non-motor) sectors. White and Brown goods are often financed through linked credit agreements. In the motor dealership, the finance product is always linked to the purchase of the car. Its selection takes into account the customer's expectations, his budget, the business or personal use of his car and is based on consumers long-term investment approach to motor acquisition rather than buying on impulse. Motor finance at the point of sale is characterised by being accessible to many consumers (high acceptance rate) and safe for consumers (low cost of risk).

Store and Credit Card

Distribution of credit at the point of sale may be performed through store or credit cards.

A basic store card typically has a limited acceptance network which corresponds to limited purchase abilities.

The store card offers a revolving credit facility without a fixed end date. Repayment, which may be made in full or based on a fixed percentage or amount per month, is monthly based.

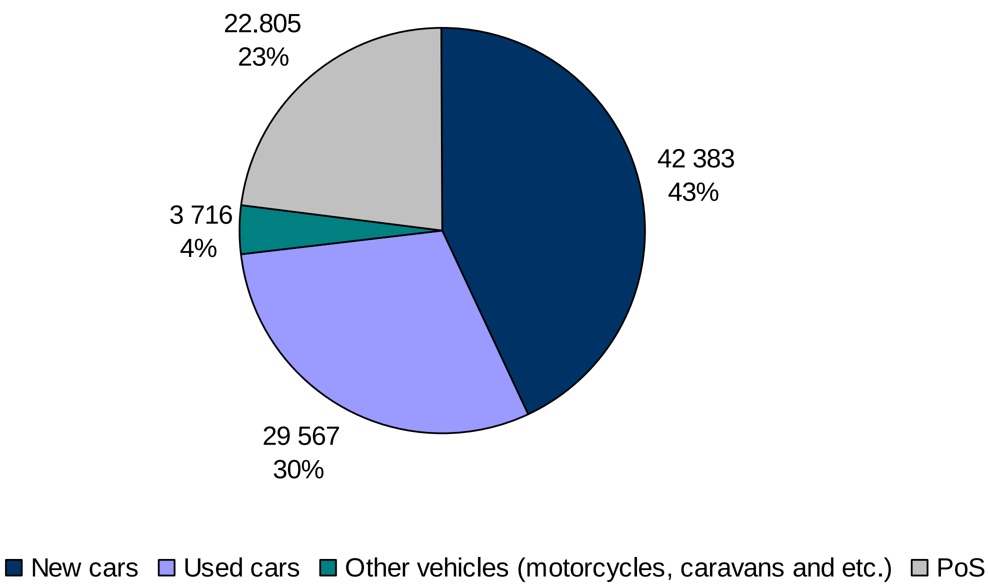
<u>Store cards are characterised by a low frequency of transactions, low limits and relatively low balances</u>.

A credit card may offer an ATM access and can be co-branded VISA/MasterCard. In this latter case, the purchase possibility is extended thanks to the existence of a worldwide acceptance network.

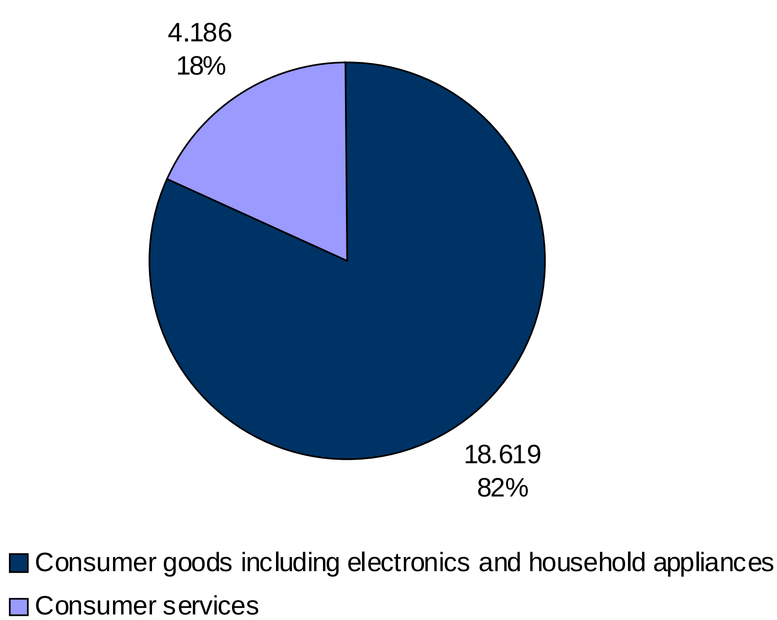
White and Brown goods can be financed through store or credit cards.

iv) Typical Goods and Services financed at PoS

Point of Sale Finance by product type in 2008 (in mil€)



Point of Sale Finance for Goods and Services in 2008 (in mil€)



In 2007, new credit granted by Eurofinas member companies for consumer goods including electronics and household appliances amounted to €19.3 billion. This represented 82% of the new credit financed at the point of sale for all goods and services. The remainder of the new credit granted was for other consumer services which accounted for €4.3 billion of point of sale credit for goods and services.

Total Vehicle Finance in 2008		
	New credit granted in mil€	% change to previous year
Passenger Cars		
Private	71,950	-12,3%
Business	16,601	-8.4%
Passenger Cars		
New	42,383	-15.7%
Used	29,567	-7.5%
Commercial Vehicles	9,656	-8.5%
Other (caravan, motorcycles, etc.)	3,716	-15.6%
Eurofinas	**101,922**	**-11.7%**

In 2007, new credit granted for the purchase of new passenger cars increased by 1.8% and amounted to €62.3 billion.

81.8% of new credit granted was to finance passenger cars destined for private use. The rest of the credit was granted to businesses.

PoS finance is of strategic importance to the sectors represented by Eurofinas. Consumers often request finance when purchasing a good or a service at the point of sale. **Specialised consumer credit providers have therefore developed PoS finance processes to meet consumer's needs.**

II. HOW DOES POS FINANCE WORK?

i) Lender's selection of credit intermediaries

A careful selection of retailers and motor dealers, using all available data, is conducted by lenders to ensure high-quality partnerships.

In order to create a commercial partnership with a retailer or a motor dealer, lenders will typically analyse extensive data such as solvency, reputation as well as the overall working and trading environment of the store/motor dealership. Only after this will the lender proposes a commercial partnership. The details for negotiation will include the nature of the partnership (exclusive or non exclusive), its duration and how products are priced. This relationship may be restricted to a single independent store/motor dealership or extended to wider distribution network in case of national or international chain stores.

There is no general rule in relation to the exclusivity of agreements.

The selection process usually involves a pilot phase which will confirm the viability of the partnership. Commercial partnerships between lenders and retailers/motor dealers are reviewed regularly by both parties. Such agreements can be revoked in the event of misconduct of the retailer/motor dealer.

Specificities of the automotive sector

Motor dealers are carefully recruited based on rigorous scrutiny of all available data to ensure high-quality partnerships. Sometimes lenders operate through motor dealerships' franchised networks. This is notably the case for captive finance companies of car manufacturers.

Business managers are often specifically recruited to deal with credit applications.

Motor dealers are usually not tied to a finance company and typically work at least with more than one lender. This enables consumers to have a wider choice in terms of products when requesting a finance solution at the point of sale for the purchase of their car.

ii) Lenders' monitoring of credit intermediaries'

Lenders closely monitor retailers and motor dealers from the start of a relationship. This process is on-going and includes visits of the store/motor dealership and regular business reviews. Periodical statistical risk analysis is produced in collaboration with the store/motor dealership. In addition, regular assessments of retailers/motor dealers are conducted. *Ad hoc* checks are also performed by lenders as often as deemed necessary.

These procedures enable lenders to adapt quickly, for example to make the required changes to training programmes or to identify problem with fraudulent applications.

iii) Lenders' assistance and support to credit intermediaries

Lenders first have to make sure that retailers/motor dealers comply with all the components of the credit application process. The former will offer assistance to immediately remedy any shortcomings. In addition, lenders need to assess and understand retailers/motor dealers' expectations which comprise the i) speed of credit decision and the offer, ii) regular visits by lenders' representatives to the point of sale, iii) advertising and legal support and iv) bespoke training sessions.

All contracts, products and processes are created and approved by lenders in accordance with the relevant legislation in force. Retailers/motor dealers play no part in this. It is their contractual duty to respect lenders' processes and to circulate all pre-approved documentation to borrowers.

As mentioned above, **any breach of the agreement by retailers / motor dealers could lead to the termination of the partnership**.

It is the lenders' responsibility to comply with all potential legal changes in consumer credit pre-contractual and contractual information, credit products or advertising practices and to make all appropriate modifications to their offers at the point of sale. Retailers/motor dealers are informed of the legal changes and all materials are accordingly updated by lenders. The involvement of lenders in informing and explaining legal changes is essential for retailers/motor dealers' understanding.

All marketing and advertising materials are reviewed if not provided by lenders. The review includes legal and compliance checks by lenders' legal department.

In order to assist their partners, all lenders have dedicated teams to support retailers/motor dealers in their PoS finance activity. This results in high quality services being provided to customers. Lenders usually provide a dedicated hotline for dealers. This acts as a help desk for queries relating to products, commercial campaigns and credit decisions as well as handling dealers' requests for marketing material.

A senior manager is tasked with:

- monitoring the progress of the retailers/motor dealers;
- providing training;
- explaining business systems, include IT
- ensuring that dealers' regulatory knowledge is up-to-date ; and
- helping organise special events.

This builds a confident working relationship between the lender and the retailer/motor dealer.

iv) Lenders' training of credit intermediaries

The wide variety of retailers and motor dealers and environment differences require lenders to deliver customised training programs that lenders are best placed to provide. This is key to adapt to fraudulent techniques which are constantly evolving.

The senior manager is usually responsible for the successful implementation of training programs. These ones may comprise a combination of on-site and online training and will include a focus on how products work and their key features and pre-contractual information (including APRC). In addition, the lender helps retailers and motor dealers to spot fraudulent identity or income documents. The lender ensures that the necessary training is always available.

v) Credit intermediaries' role and duties

If a consumer requests finance at the point of sale, retailers/motor dealers will inform them about how the product works and its key features. Pre-contractual information is provided by retailers/motor dealers to consumers on behalf of the lender.

Information on product features and functioning is available at all stage (description of each product along with potential supporting documents). **Retailers/motor dealers do not provide advice to consumers.**

The credit application process is completed by the retailer/motor dealer via an online application or through a standardised application form. In the latter circumstance, the retailer/motor dealer has to call the lender for decision or fax the application form. Both application processes are underpinned by training and testing programmes, regulatory requirements and regular controls. Given their speed, efficiency and built-in security, online applications tend to be the preferred working method of lenders and retailers/motor dealers.

The retailer will usually have to connect to the online application form by filling in his store identification number and his personal employee identification number. Such a step is often required in big chain stores where several dedicated staff can be in charge of PoS finance in order for the lender to ensure a complete overview of the credit applications.

The retailer will then collect numerous data including, *inter alia*, the customer's ID number, identity, address and home phone number. Accuracy of information will be checked by lenders once the application has been completed. In other cases, the latest online application tools instantly confirm whether the ID number and the address are valid and linked to the applicant. In such cases, should the data be incorrect, the system will not allow the retailer to continue the online application process unless the data is changed.

All the information collected on the applicant is checked by the lender before any credit decision is made, whether this is done instantly via online application or later on as if it is conducted via another channel.

The ability to repay and/or the credit limit are never driven by the retailer but by the lender (through IT scoreboards). **Retailers play no role in the credit granting decision**.

If the application is accepted, the retailer will give the customer a contract for agreement and signature.

Borrowers address any finance-related questions directly to the lender. This could include additional information on products or procedures, to complain or in case of any difficulties arising during the duration of the contract. Lenders are responsible for dealing with customer complaints, withdrawal, early settlement and debt recovery.

If the application is refused, the retailer will inform the consumer that his application has been refused. Consumers can get explanations by contacting the lender or alternatively the credit bureau to find out about their credit history file.

Online application processes tend to be the norm. High automation responds to the need for speed, quality of decision and operational risks management. **The fact that a credit decision is taken quickly does not mean that lenders are not behaving responsibly.** This is because the credit decision process includes very high volumes of checks. Hence **the speed of the credit decision has no impact on its quality.**

It should be remembered that retailers and motor dealers practise credit mediation as an ancillary activity and receive no fee from consumers.

As acknowledged in Europe Economics study on Credit Intermediaries in the Internal Market, the benefits of PoS finance are numerous[13].

PoS finance facilitates consumers' access to goods and services.

PoS finance is often a starting point for establishing and developing a consumer credit market, particularly in non-mature markets. It allows consumers to develop a credit history and finance previously inaccessible goods. This contributes to an improved standard of living. In this context, clients acquired by lenders through merchants represent an opportunity to convert them into direct customers.

PoS finance enhances consumption to fuel the economy.

Finance products offered at the point of sale can be tailored to meet consumers' needs. For instance products offered at a motor dealer's showroom would typically be adjusted to the customer's use of his vehicle. PoS finance allows a retailer or a motor dealer to become a "one-stop shop" for the consumer. These products often represent better value packages for the consumer than in branches.[14]

Point of sale finance enables specialised credit providers to reach out to a large customer base.

According to the Europe Economics study, "these institutions are heavily dependent upon point of sale as a distribution channel for their credit products". This is because many specialised institutions do not have a substantial branch network or may even lack branches altogether.

The importance and advantages of the distribution of credit at the point of sale (for the economy and all the parties involved, including consumers) should not be ignored overlooked by decision-makers.

Given the role dealers play in the distribution of consumer credit at the point of sale, Eurofinas strongly believes that it would be inequitable to subject them to the same requirements as credit brokers. Furthermore, it is unclear how credit consumers would gain further benefits from retailers and motor dealers being regulated in addition to the existing provisions applying to lenders under the new CCD.

Eurofinas believes that subjecting retailers and motor dealers to the same requirements as credit brokers would inhibit the supply of sustainable credit, particularly to those most in need.

It is worth emphasizing the large number of dealers involved in the distribution of (consumer) credit at the point of sale and the extreme difficulty there would be in implementing any type of regulatory regime for retailers/motor dealers. This would drive up costs and invariably penalize the consumers (higher prices or dealers getting out of that ancillary activity).

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[13] *See Europe Economics,* Study on Credit Intermediaries in the Internal Market*, p. 150*

[14] *See Europe Economics,* Study on Credit Intermediaries in the Internal Market, *reference to Bertola et al. (2005) "when financing is potentially available to enable the purchase of the product, it is typically offered at interest rates lower than those available in the direct market", p. 150*

Eurofinas believes that the nature of the agreement between the lender and its intermediary (i.e. exclusive or non-exclusive partnerships) is irrelevant in the context of PoS finance. The Europe Economics study found that in some of the larger Member States, lenders supported their PoS partners irrespective of whether the partnership was exclusive. Examples included product-specific training and marketing and IT support.

As regards other forms of credit mediation, the Federation believes that a distinction should be made between:

i) intermediaries who are neutral third parties that are not contractually linked with one or several credit providers (untied intermediaries) and,
ii) intermediaries having a contractual relationship with one or several credit providers who are, in turn, responsible for the activities performed by their tied agents.

.
Tied intermediaries are encompassed within the regulatory provisions to which lenders are subject.

In this context, the Federation wishes to draw the attention of the Commission on potential detrimental effects of further regulatory constraints which could drive up costs for lenders, lead to revocation of partnerships and challenge the distribution of small amount loans (which is of particular importance in the field of consumer credit).

Eurofinas therefore wishes to emphasize the importance of an in-depth analysis of the legal implications of the above-mentioned distinction.

Question 10: *Could you give examples of cases of misconduct, mis-selling or any other instances of consumer detriment linked to credit intermediaries in your country?*

The distribution of credit at the point of sale is always based on a clear allocation of responsibilities between parties. On the one hand, the retailer/motor dealer, who is tasked with gathering all required data, must inform customers about the credit facilities, contractual agreements and product features. The retailer has no responsibilities or influence on the credit decision. In contrast, the credit provider who has exclusive ownership of credit policy, credit decision and follow-up of credit files, is charged with checking all data. They must also ensure that retailers and motor dealers are made aware of the latest developments, including via training and keep borrowers informed.

Eurofinas strongly believes that current European and National regulatory frameworks, along with credit providers' strict control and supervision of retailers and motor dealers involved in the distribution of credit at the point of sale, effectively prevent cases of misconduct or mis-selling.

Direct fraud

Retailers and motor dealers have no flexibility to derogate from lenders' supervision. **Any serious misbehaviour leads to the revocation of the agreement between the lender and its partner**.

This has been confirmed by Europe Economics in its study on Credit Intermediaries in the Internal Market. The consultancy acknowledges that few specific real-life cases of consumer detriment related to PoS intermediation have been identified[15] and that credit providers will continue to strongly impact PoS intermediary behaviour in the absence of significant regulation[16].

Direct fraud by credit intermediaries at the point of sale is limited. As recognized by Europe Economics, intermediaries' scope for direct fraud may be limited with PoS credit provision, mainly because the contract is usually processed from beginning to end in front of the consumer within a tight deadline.

Additionally, it is worth highlighting that direct fraud by the intermediary was not considered by the consultancy to correlate to the intensity of regulation. In the context of PoS finance, direct fraud is not perceived to be a major source of consumer detriment[17].

Transparency

The Europe Economics study states that consumers may face difficulties in identifying and understanding all consumer credit contracts conditions. Eurofinas understands such a concern and believes that any potential consumers' detriment arising from the transparency of the offer will be resolved by the implementation of the CCD's provisions on pre-contractual information and the duty to provide adequate explanations.Europe Economics found greater likelihood of detriment when credit intermediaries offered advice[18]. This is why Eurofinas believes that advice mechanisms at the point of sale are unsuitable.

[15] See Europe Economics, *Study on Credit Intermediaries in the Internal Market*, p. 177
[16] See Europe Economics, *op.cit.*, p. 174
[17] See Europe Economics, *op.cit.*, p. 176
[18] See Europe Economics, *op.cit.*, p. 54

Question 11: *Does the regulatory patchwork for credit intermediaries present a problem in your view?*

As mentioned in Europe Economics study, there is currently limited explicit statutory regulation of PoS intermediaries across Europe.

Eurofinas believes that far from creating a legal gap it reflects a common approach according to which retailers and motor dealers involved in the distribution of credit at the point of sale are considered to act under the full responsibility of credit providers. **This is because all regulatory provisions to which consumer credit providers are subjected are necessarily reflected at the point of sale.** It is the lenders' responsibility to comply with all potential legal changes in consumer credit pre-contractual and contractual information, credit products or advertising practices and to make all appropriate modification to their offers at the point of sale. Retailers and motor dealers are informed of the legal changes and all materials are accordingly updated by lenders.

Retailers and motor dealers have no flexibility to derogate from lenders supervision. Any serious misbehaviour leads to the revocation of the agreement between the lender and its partner.

Cross-border activities

Eurofinas would like to recall some of the findings of the study on the legal and economic impact of Directive 2002/65/EC of the Distance Marketing of Consumer Financial Services.

The study found that less than five retail banks in the entire EU, actively conducted direct cross-border distance marketing as a primary business strategy. The market for these services is extremely small (less than 0.1% of total consumer credit transactions take place across different Member States). The current market is very fragmented as there is very little consumer and provider participation in cross-border financial trade. This is for a number of practical reasons.

On the demand side these include i) **consumers' preference for national providers** as they intrinsically trust their 'own' consumer credit providers, ii) **language and cultural differences** which make it more complex to deliver popular consumer credit products uniformly across the EU and iii) **excessive/incomprehensible information** given to consumers, which they cannot understand (as an effect of the Directive 2002/65/EC of the Distance Marketing of Consumer Financial Services).

On the supply side, barriers include **anti-money laundering requirements** which prevent the convenient trade in cross border consumer financial products and **cross-border debt recovery processes** which are legally uncertain and complex.

PoS finance plays an important role in increasing competition and the development of the Single Market. It allows specialised credit providers to serve an important customer base. It greatly contributes to the growth and expansion of credit and consumption goods distribution in the EU.

The idea that PoS finance may facilitate the provision of consumer credit cross-border is theoretical. In practice, most credit providers do cross-border business by creating local subsidiaries or branches in other European markets. The role of PoS finance in the development of direct cross-border credit has, therefore, still to be demonstrated. Because PoS finance is intrinsically a local activity, it would not benefit from a single European passporting regime.

Question 12: *What would be the most appropriate way to address potential conflicts of interest, particularly with regard to fee/bonus/commission structures? Should any measures in this regard apply to bank client-facing staff as well as intermediaries?*

As mentioned in the consultation paper, article 21 of the CCD requires credit intermediaries to indicate in advertising and documentation intended for consumers the extent of their powers, in particular whether he works exclusively with one or more creditors or as an independent broker.

This provision applies to retailers and motor dealers active in the distribution of credit at the point of sale. This means that retailers and dealers will indicate to consumers the number of lenders with whom they have a partnership.

Eurofinas notes the Commission's interest in ensuring the disclosure of information of the specific fees payable by the borrower to the intermediary for the provision of the service. Article 21 of the CCD requires credit intermediaries to inform applicant borrowers of the fees payable by the consumer to the intermediary for his service.

Retailers and motor dealers do not receive any payments from borrowers for the provision of credit at the point of sale.

As regards PoS finance, remuneration of intermediaries reflects the services rendered by retailers and motor dealers to lenders. Credit intermediaries' commission is not charged separately to borrowers and is taken into account in lenders pricing.

As regards potential conflicts of interest with regard to commission structures, though Europe Economics concluded that "there exists a structural inefficiency in performing tasks aimed at alleviating asymmetric information where the main mode of remuneration is a volume-based commission", PoS intermediation was however considered to be qualitatively different in this regard from other areas.

As mentioned by the consultancy, in comparison with other forms of credit mediation "the scope for a conflict of interest is absent for point of sale intermediaries"[19].

In order to test the robustness of its conclusion, the consultancy checked its predictions with information collected through its survey of consumer associations about the perceived risk of consumer detriment arising from recommendations of inappropriate products or non-competitive products.

It was concluded that, as regards PoS finance, the limited risk perceived by consumer associations was to be explained as <u>a consequence of a restricted market-search activity by consumers</u>.

Eurofinas agrees with Europe Economics' findings and believes that the risk of potential conflict of interest due to PoS intermediaries' remuneration schemes is extremely limited.

[19] See Europe Economics, *op.cit*., p. 58

Question 13: *What are your views on the registration and supervision of credit intermediaries?*
Question 14: *What are your views on prudential and professional requirements for credit intermediaries (such as minimum capita, professional indemnity insurance, educational or professional qualifications)?*

Eurofinas understands the Commission's concern to ensure that credit intermediaries are appropriately regulated. However, as previously mentioned, retailers and motor dealers involved in the distribution of credit at the point of sale have no flexibility to derogate from lenders supervision. **Any serious misbehaviour leads to the revocation of the agreement between the lender and its partner**.

The Commission's consultation paper considers various approaches for possible supervision:

- ***enabling supervisory authorities to assess whether intermediaries are involved in the provision of high risk credit***

Retailers and motor dealers involved in the distribution of credit at the point of sale are not involved in the provision of high risk credit. Their role consists in providing a consumer credit loans (e.g. automotive finance, linked credit, store/credit cards) to consumers who request finance at the point of sale.

- ***helping to give borrowers confidence that the intermediary has suitable qualifications and expertise, and that there is an authority to which they could turn in the event of a dispute.***

Retailers and motor dealers **involved in the distribution of credit at the point of sale are not entitled to advise applicant borrowers.** Any dispute arising between the intermediary and a consumer will be settled by the lender, if necessary using an alternative dispute resolution (ADR) scheme[20].

Eurofinas agrees with the Commission that appropriate qualifications of intermediaries are important. In this context the Federation would like to stress that retailers and motor dealers training is at the heart of PoS finance business model. The wide variety of retailers/motor dealers and environment differences require customised training programs that lenders are best placed to provide.

The senior manager is usually responsible for the successful implementation of training programmes. These ones may comprise a combination of on-site and online training and will include a focus on how products work and their key features and pre-contractual information (including APRC). In addition, the lender helps retailers and motor dealers to spot fraudulent identity or income documents. The lender ensures that the necessary training is always available.

- ***creating a level playing field between intermediaries at the EU level and opening up the possibility to provide cross-border intermediation services under a 'passport' system***

[20] See Eurofinas response to question 15 on the applicability of lenders ADR to PoS finance

Given the role **retailers and motor dealers** play in the distribution of consumer credit at the point of sale**,** these ones **would, by definition, not benefit from a single European passporting regime.**

- ***providing a basis on which to determine the authorisation of access by intermediaries to borrowers' credit data***

As regards point of sale finance, **intermediaries do not access borrower's credit data as they do not carry out creditworthiness assessments themselves**. All the information collected on the applicant is checked by the lender before any credit decision is made, whether this is done instantly online application or later on as is this the case through other channels.

Borrower's ability to repay the loan or the credit limit is never driven by the intermediary but by the lender. Intermediaries play no role in the credit granting decision.

In light of the elements mentioned above, **Eurofinas strongly believes that prudential and supervision requirements for retailers and motor dealers involved in the distribution of credit at the point of sale are unnecessary.**

In addition, it is worth emphasizing the very high number of dealers involved in the distribution of (consumer) credit at the point of sale and the extreme difficulty there would be in implementing any type of regulatory regime for retailers/motor dealers. This would drive up costs and invariably penalize the consumers (higher prices or dealers getting out of that ancillary activity).

Insurance Mediation Directive

Eurofinas would like to highlight the extreme difficulty (given the high number of retailers/motor dealers involved) there would be on implementing any type of regulatory regime for retailers/motor dealers. The implementation of the Insurance Mediation Directive (IMD) should be used in that respect as a precedent.

Effects of IMD's implementation in several markets include:

- a significant increase in costs (ultimately passed on consumers) caused by an increased administrative burden on lenders;
- a decrease in sales volumes;
- the withdrawal of some insurance products from the market; and
- the revocation of partnerships by smaller sized intermediaries due to excessive regulatory requirements imposed on them.

Eurofinas believes that some of the negative impacts of the Insurance Mediation Directive could have been avoided by taking better into consideration the level of responsibility of different types of insurance intermediaries.

Eurofinas believes that applying the same requirements to retailers and motor dealers as for credit brokers would be disproportionate and inequitable given their limited role in the distribution of consumer credit at the point of sale.

Eurofinas believes that applying the same requirements to retailers and motor dealers as for credit brokers would be disproportionate and inequitable given their limited role in the distribution of consumer credit at the point of sale.

EC Question 15: *How do you think the activities of credit intermediaries could be brought within existing complaints and out-of-court redress mechanisms?*

Eurofinas agrees with the Commission that out-of-court redress systems ensure that consumers have means to settle potential disputes with their providers without the need for long and costly court procedures.

Eurofinas therefore strongly supports the promotion of out-of-court settlement mechanisms that comply with the principles of impartiality, transparency**,** effectiveness and fairness. The nature of out-of-court bodies involved in the resolution of these disputes (private, public bodies) and funding methods are irrelevant as long as these bodies comply with the above-mentioned principles.

As regards consumer credit, the Federation wishes to highlight that according to article 24 of the CCD Member States should ensure that adequate and effective out-of-court dispute resolution procedures for the settlement of consumer disputes concerning credit agreements are put in place.

This means that, as regards consumer credit, ADR schemes should be operational in all Member States by 11 June 2010[21].

Given the role retailers and motor dealers play in the distribution of consumer credit at the point of sale**,** any disputes arising from the distribution of credit at the point of sale will involve the credit provider and therefore benefit from the ADR schemes in place. The Federation therefore believe that there is no need to promote further out-of-court mechanisms for PoS finance.

In addition, it is worth highlighting that under article 15 of the CCD (as regards linked credit agreements which are *de facto* mainly granted at the point of sale), the borrower has the right to pursue remedies against the lender when he has failed to obtain satisfaction to which he is entitled for the supply of goods or services.

Eurofinas believes that, in all cases, particular attention should be provided to the follow-up of the Commission's 1998 Recommendation *on the principles applicable to the bodies responsible for the out-of-court settlements of consumer disputes* and 2001 Recommendation on *the principles for out-of court bodies involved in the consensual resolution of consumer*.

Other forms of credit mediation (i.e. brokers and the like), are already covered by ADR mechanisms in several markets. Eurofinas therefore recommends that the Commission carries out a preliminary assessment in order to identify in which Member States such procedures are already in place (whether or not via regulation).

[21] According to Article 24 of the CCD, existing bodies may be used where appropriate.