

European Communities

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EUROPEAN PARLIAMENT

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## Report

drawn up on behalf of the Legal Affairs Committee

**on the proposal from the Commission of the European Communities to the Council (Doc. 10/79) for a directive relating to the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit**

**Rapporteur: Mr C.J. PROUT**

By letter of 16 March 1979 the President of the Council of the European Communities requested the European Parliament pursuant to Article 100 of the EEC Treaty, to deliver an opinion on the proposal from the Commission of the European Communities for a directive relating to the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit.

On 30 May 1979 the President of the European Parliament referred to the Legal Affairs Committee as the committee responsible and to the Committee on the Environment, Public Health and Consumer Protection for its opinion.

On 10 October 1979 the Legal Affairs Committee appointed Ms Vayssade rapporteur.

On 20 November 1979 the committee examined the proposal for a directive in the light of an introductory statement by the rapporteur. At its meeting of 27-28 March 1980 the committee noted that 67 amendments had been tabled to the draft report (PE 59.430); it decided to postpone consideration and adoption of the draft report in order to study them in detail.

On 28 April 1980 the committee first considered Amendment No.1 by Mr Prout, Mr Megahy and Mr Goppel, which questioned the existence of a legal basis in the EEC Treaty for the proposal. The amendment was adopted<sup>1</sup>, with 10 votes for, 7 against and 2 abstentions. Since the text of the amendment replaced the motion for a resolution in its entirety, the committee took no further votes on the draft report or on the amendments.

In view of the committee's decision, Ms Vayssade asked to be replaced as rapporteur. On the chairman's proposal, Mr Prout, first signatory of the amendment, was appointed in her stead. The committee instructed the new rapporteur to draft the accompanying explanatory statement to reflect the committee's views.

In the explanatory statement, which also contains a statement of the views of the minority pursuant to Rule 42(2) of the Rules of Procedure, the rapporteur has drawn on the views expressed in committee at the meetings of 20 November 1979 and 28 April 1980.

The opinion of the Committee on the Environment, Public Health and Consumer Protection is annexed to this report.

1 Present : Mr Ferri, chairman, Ms Vayssade, first rapporteur, Mr Prout second rapporteur, Mr Chambeiron, Lady Elles (replacing Mr Turner), Mrs Ewing, Mr Geurtsen, Mr Gillot, Mr Gonella, Mr Henckens (replacing Mr Modiano), Ms Hooper (replacing Mr Dalziel), Mr Janssen van Raay, Mr Luster, Ms Macciocchi, Mr Malangre, Mr Pelikan, Mr Peters (replacing Mr Vetter), Mr Sieglerschmidt, Mr Tyrrell

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A.

The Legal Affairs Committee hereby submits to the European Parliament the following motion for a resolution, together with explanatory statement:

MOTION FOR A RESOLUTION

embodying the opinion of the European Parliament on the proposal from the Commission of the European Communities to the Council for a directive relating to the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit

The European Parliament,

- Having regard to the proposal from the Commission of the European Communities to the Council,<sup>1</sup>
  - Having been consulted by the Council pursuant to Article 100 of the EEC Treaty (Doc. 10/79),
  - Having regard to the report of the Legal Affairs Committee and the opinion of the Committee on the Environment, Public Health and Consumer Protection (Doc. 1-161/80),
1. Considers that the existence of a legal basis in the EEC Treaty for this proposal has not been justified;
  2. Requests consequently the Commission to withdraw its proposal.

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<sup>1</sup> O.J. C 80 of 27.3.79, p.4

B.

EXPLANATORY STATEMENT

I. INTRODUCTION

1. The Commission have chosen Article 100 of the Treaty of Rome as the sole basis for their draft proposal. The relevant part of the Article reads as follows:

'The Council shall...issue directives for the approximation of such provisions laid down by law, regulation or administrative action in Member States as directly affect the establishment or functioning of the common market.'

To apply this Article, three factors must be present. First, the provisions of the Member States it is proposed to approximate must 'directly affect the establishment or functioning of the common market'. Second, the Community directive must represent an 'approximation of such provisions laid down by law, regulation or administrative action in Member States'. Third, the effect of approximation by Community directive should be to eliminate the harmful effects caused by disparities between the anterior provisions.

II. OPINION OF THE EUROPEAN COMMISSION

2. The Commission set out the case for the use of Article 100 in the recitals of the proposal as follows:

'Whereas wide differences exist between the laws in force in the Member States of the European Economic Community in matters of consumer credit;

Whereas these differences in the national legal provisions are liable to jeopardise the establishment of a system which ensures that competition between creditors is not distorted in the common market;

Whereas these differences lead to disparities in the degree of consumer protection in the various Member States, limit the opportunities the consumer has to obtain credit in another Member State, affect the volume and the nature of the credit sought, and also the purchase of goods and services;

Whereas, in consequence, these differences have an influence on the free movement of goods and services obtained on credit and thus hinder the harmonious development of economic activities throughout the Community;

Whereas the Preliminary Programme of the European Economic Community for a consumer protection and information policy provides, inter alia, that the consumer should be protected from unfair credit terms and that a harmonization of the general conditions governing consumer credit should be undertaken as a priority; whereas for the foregoing reasons the laws in force in Member States concerning consumer credit directly affect the functioning of the common market;'

3. Similar arguments are advanced in paragraphs 13 and 14 of the Explanatory Memorandum.

4. When giving evidence to the committee, the Commission argued that the provision of consumer credit related directly to the Common Market and that the differences in existing national laws thus adversely affected the functioning of the Common Market. As an alternative argument, the Commission expressed the view that the proposal should be seen as a step towards the creation of a Common Market in credit. The Commission representatives cited the views of a number of organisations (including the OECD) in favour of coordination of legislation at European level. The Commission said, however, that it was not possible to obtain statistical evidence as to the effect of the differences between national legislations on the Common Market.

### III. OPINION OF THE LEGAL AFFAIRS COMMITTEE

5. The majority of the Legal Affairs Committee consider that the legal basis chosen has not been justified. It is appropriate to consider each recital in turn in the light of the additional written and oral evidence by the Commission to the committee.

6. The first recital asserts that there are 'wide differences' between the consumer credit laws of Member States. Chapter II of the Explanatory Memorandum provides a brief summary of the legal position in each State. But no attempt whatsoever is made to analyse comparatively the differing national provisions on consumer credit and the way in which they are applied in order to justify the contention that 'wide differences' exist between them, despite repeated requests by the Legal Affairs Committee that such an analysis be made.

7. The second recital asserts that the differences between national provisions on consumer credit are 'liable to jeopardize the establishment of a system which ensures that competition between creditors is not distorted in the common market.' This calls for a number of observations. First, if the object of the draft proposal really is to assist in establishing a 'system which ensures that competition between creditors is not distorted in the common market', then the vast majority of its clauses, directed as they are to the protection of the consumer, are either irrelevant or unnecessary or counter-productive. Moreover, it seems extraordinary that consumer credit should be singled out from all the other markets in credit for preferential treatment in achieving this objective. Any initiative on a system to ensure free competition between creditors ought anyway to be taken under Articles 67-73 of the Treaty. Second, the Commission has brought forward no statistical or other evidence whatsoever to support the assertion that national legislative divergencies are liable to jeopardise the establishment of such a system, despite repeated requests to them to do so.

8. Third, were such evidence to be forthcoming it is doubtful whether it is sufficient to demonstrate that the establishment of such a system is 'liable to be jeopardised' by any existing differences. It is highly likely that Article 100 requires that the establishment of such a system is jeopardised by existing differences. Finally, Article 100 requires that the effect that the national differences produces upon the establishment of the common market is direct. The meaning of the word 'direct' in this context has been the subject of some debate. Broadly speaking, there are two approaches. Those who favour a literal interpretation say that an immediate causal link between divergent national legislation and distortions in the common market must be shown<sup>1</sup>. Those who take a broader approach insist merely that there should be certain intensity of effect<sup>2</sup>. But it unnecessary to take a position on the relative merits of the two views on this occasion because the Commission has failed to demonstrate a link of any sort between divergencies and distortion.

9. The third and fourth recitals read together put forward an alternative justification for the legal basis chosen. By creating 'disparities in the degree of consumer protection', by 'limiting the opportunities the consumer has to obtain credit in another Member State' and by 'affecting the volume and the nature of the credit sought', national divergences in legislation 'have an influence on the free movement of goods and services obtained on credit'. This argument invites a number of observations. First, once again no evidence whatsoever has been advanced for any one of these numerous causal propositions. Second, it has already been observed that, at least in one view, there must be an immediate causal link between the divergences, on the one hand, and the functioning of the common market, in this case the market in goods, on the other. Yet in recitals 3 and 4 the causal links between the two are manifestly indirect!

10. Third, it is extremely unlikely that Article 100 applies to the 'free movement of goods and services'. Title I of the EEC Treaty, comprising Articles 9-37, provides a comprehensive scheme for the establishment and functioning of the Common Market in goods and services. In particular, it provides for 'the elimination of quantitative restrictions between the Member States and all measures having equivalent effect'. If the concern of the Commission is that divergent rules on consumer credit interfere

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1 See House of Lords, Select Committee on the European Communities, Session 1977-1978 22nd Report, Approximation of Laws under Article 100 of the EEC Treaty, pp. 9-10

2 See 'Community Policy with Regard to the Approximation of Laws', lecture given at Edinburgh, 18 November 1977 by C.-D. Ehlermann, Director-General, Legal Service of the Commission of the European Communities, esp. p.47

with inter-State movement of goods and services, then they should be dealt with as measures having an 'equivalent effect'.

11. The fifth recital refers to the 1975 Preliminary Consumer Protection Programme of the EEC in support of the view that harmonisation of the general conditions concerning consumer credit should be undertaken as a priority. But this reference is of little value because the Programme itself cannot be used as the legal basis for harmonisation. The protection of the consumer is not one of the purposes expressly provided for in the Treaty and the declarations contained in the Preliminary Consumer Protection Programme cannot extend its legal scope.

12. It has been argued that since the Programme was unanimously adopted by the Council of Ministers the limits of the Treaty were validly extended. But this view is fallacious. By signing the Treaty of Rome and incorporating its terms into their domestic law Member States effectively transferred a part of their sovereignty to the European Community. But the extent of this transfer was fixed and determined by the Treaty. The Council of Ministers, like any other Community institution, is constrained by the terms of the Treaty and cannot extend the degree of sovereignty transferred from Member States to Community competence even by unanimous voting. This can only be done by invoking the proper amendment procedures laid down in the Treaty.

13. At the end of the fifth recital the Commission states that 'for the foregoing reasons the laws in force in Member States concerning consumer credit directly affect the functioning of the common market'. The committee's view is that the direct effect has not been demonstrated by the Commission, either in the proposal's recitals or elsewhere. It therefore considers that the legal basis for the proposal has not been justified.

14. In these circumstances it is necessary to consider only briefly the other two factors, mentioned in the introduction of this report, which must be present for Article 100 to apply. First, the proposal must represent an 'approximation of such provisions laid down by law, regulations or administrative action in Member States'. Yet a number of clauses in the proposal appear to impose standards exceeding those required by any of the existing national rules in Member States. Now there may be circumstances in which such raising of standards is necessary to the process of approximation. But, again, the justification is absent from the recitals or explanatory memoranda of the proposal.

15. Second, the effect of approximation by the proposal must be to eliminate the harmful effects caused by disparities between the anterior provisions. Again little purpose is served by elaborating this point in great detail.



The committee will, therefore, confine itself to two brief but fundamental observations. The first is that the Commission does not propose to harmonise the method of calculation of the effective annual rate of interest. Yet accurate information as to interest rates is crucial for the consumer. If it is considered necessary to approximate national provisions on consumer credit in order to protect consumers throughout the Community this key aspect cannot be excluded. Without it there is no true approximation. The second relates to Article 16, which permits Member States to introduce or retain more stringent provisions to protect consumers than are contained in the proposal. Article 16 will inevitably lead to the same divergences that the proposed directive purports to eliminate!

#### IV. CONCLUSION

16. The Legal Affairs Committee has concluded that the case for the use of Article 100 of the EEC Treaty has not been proved. It has therefore decided that the best course of action would be to ask the Commission to withdraw its proposal.

APPENDIX

OPINION OF THE MINORITY OF THE LEGAL AFFAIRS COMMITTEE

The minority of the Legal Affairs Committee, including the first rapporteur, Ms VAYSSADE, is of the view that action should be taken at Community level to harmonise Member States' laws on consumer credit in order to ensure that consumers throughout the Community are adequately protected. They consider that the Commission has presented sufficient evidence and has made out a convincing case for the use of Article 100.

OPINION OF  
THE COMMITTEE ON THE ENVIRONMENT, PUBLIC HEALTH AND CONSUMER PROTECTION

Draftsman: Mrs V. SQUARCIALUPI

On 25 September 1979 the Committee on the Environment, Public Health and Consumer Protection appointed Mrs Vera SQUARCIALUPI draftsman.

It considered the draft opinion at its meetings of 24 and 25 January and 28 February 1980 and adopted it at the latter meeting by 8 votes to 3 with 4 abstentions.

Present: Mr Collins, chairman; Mr Johnson, Mrs Weber, vice-chairmen; Mr Ceravolo replacing Mr Segre, Mr Forth replacing Mr Sherlock, Miss Hooper, Mrs Maij-Weggen, Mr Mertens, Mr Muntingh, Mr Newton Dunn, Mrs Pruvot replacing Mrs Scrivener, Mrs Schleiher, Mrs Seibel-Emmerling, Mrs Spaak, and Mrs Squarcialupi.

I. EXPLANATORY STATEMENT

Whilst welcoming the Commission's proposal in general, the Committee considers that consumers' interests would be better served if certain changes could be made in the draft directive.

Credit agreements excluded from the application of the directive

Article 2 (1) (a) excludes mortgage credit from the directive on the grounds that it would be difficult to adapt the various national provisions to a general rule. The Committee cannot agree with this derogation. Because of the large sums of money involved in these credits, it is precisely in the property sector that the consumer must be better protected and informed. The differences in national legislation on other types of consumer credit are also considerable. The exclusion of mortgage credit from the proposal for a directive is therefore unjustified.

Article 2 (1) (c) excludes agreements that expire within three months. But even short-term credit agreements require legal guarantees that protect the weaker contracting party, and should therefore fall within the scope of the directive.

Contents of Agreements

Article 6 provides that credit agreements must be in writing and should contain "the essential contractual conditions" amongst which must be at least the particulars listed. These will not suffice. The agreements should also include clauses limiting the power of the stronger contracting party so that he cannot, for instance, demand immediate repayment of the funds in the event of the consumer falling into arrears. A clause should also be inserted allowing the consumer to terminate the agreement at short notice by early settlement of his obligations (as provided in Article 10). The principle of fair interest should also be established (i.e. prohibition of exorbitant rates of interest).

The compulsory clauses to be included in all types of credit agreements should also include one prohibiting compounded interest, i.e. the calculation of interest on interest. When a consumer has to pay interest on arrears, almost all creditors calculate the interest on the amount of each unpaid instalment due. The instalment, however, is made up partly of capital and partly of interest and thus the creditor demands a larger sum of money from the consumer than he would legally be entitled to if compounded interest were prohibited. All creditors therefore should calculate the interest on arrears only on the capital component of the unpaid instalment due, and should therefore specify how much of the credit is capital and how much interest. Even in countries such as Italy where compounded interest is prohibited under the Codice civile, the principle is violated:

- (a) when the consumer asks the creditor if he can repay the credit in advance;
- (b) when the creditor asks for advance repayment of the sum borrowed because the consumer is in arrears with his payments. In the latter case, creditors demand a sum that includes the interest due and future interest as well as the capital plus unpaid interest due.

The Commission proposal has omitted to make reference to optional running account agreements. These are contracts between sellers and buyers (the sellers being shops or mail order organisations). In the present wording of the directive, any purchase by the buyer on the basis of a contract would be subject to the provisions of Article 6 (the information expressly referred to in this Article must also appear in the original contract). This would unnecessarily complicate the administrative work and would cause an increase in costs without giving any benefit to the consumer or the seller. Provisions should be introduced to dispense with this obligation, possibly by making these contracts subject to regulations similar to those referred to in Article 6 (2) (b), for credit cards rather than those for credit contracts in Article 6 (2) (a).

#### Repossession of goods

The explanatory note on Article 9 states that the purpose of the article is to prevent the creditor, in the event of a delay in payment by the consumer, from recovering possession of the goods supplied on credit until he receives payment of the full instalment price, thereby depriving the consumer of use of the goods yet compelling him to pay the agreed price. This is unclear and moreover does not seem to completely accord with the text of Article 9, which is, however, also unclear. Paragraph 2 says that "Member States shall lay down rules to ensure that repossession of goods does not lead to unjustified disadvantages to any of the parties involved", and paragraph 1 which says that "A credit agreement shall cease to have effect from the time the creditor repossesses, either on the basis of a right of ownership or of any other right, the goods supplied under a credit agreement" would seem to be just such a rule, the only such therefore which would be laid down at Community level.

## General

Articles 13 and 14 are more specifically designed to provide effective consumer protection in the credit sector. Article 14, on the setting up of a body to receive consumers' complaints and institute legal proceedings on their behalf, does not however specify what its composition should be. This could be to the consumers' disadvantage when national implementing legislation is adopted.

In general, the directive lays down rules on consumer information and protection in the consumer credit sector, but provides only minimum guarantees. To provide any real protection, however, credit purchasing would have to be limited in advance by means of legal instruments that formed part of an economic policy aimed at combatting the risks of inflation.

In brief, one could be favourably disposed to extending the consumer credit system but not in an inflationary way. That is to say, the aim of increasing demand for consumer goods should be its negative effects on inflation rather than its beneficial effects on production.

Credit should not therefore be offered indiscriminately. The aim should be to facilitate transactions that have a positive influence especially as regards goods that are used to produce other goods and that are not themselves finished products.

When the banks have excess liquidity, they offer credit on easy terms. Consumers then apply for loans from the banks and incur debts. Care should be taken to ensure that consumer credit does not provide an incentive to further debt. The whole credit system should be coordinated in a comprehensive consumer protection policy. Financial backing must be provided to those who produce and not to those who squander or desire unnecessary goods.

A substantial number of members of the Committee expressed their disagreement with the ideas contained in the preceding four paragraphs and in paragraph 8 of the conclusions below. However, the Committee voted to maintain these paragraphs.

## II. CONCLUSIONS

The Committee on the Environment, Public Health and Consumer Protection therefore calls on the Legal Affairs Committee to take into account the following points in drawing up its report:

1. Mortgage credit, excluded from this directive, should be dealt with as soon as possible in a separate proposal for a directive in view of the substantial loans made in this area;

2. Agreements that expire within three months should not be excluded from the directive;
3. Special provisions should be introduced for optional running account agreements;
4. Account must also be taken of the fact that as at present drafted the directive might mean that the consumer who seeks to use a credit card would need to renegotiate or re-establish his credit agreement in respect of each individual transaction where he wishes to use the credit card, and that this would have a most detrimental effect upon consumer and trading interests;
5. The guarantees offered to the weaker contracting party are incomplete in view of:
  - (a) the fact that the financier may demand immediate repayment of the funds in the event of a delay in payment;
  - (b) the lack of provision for a clause allowing the consumer to withdraw from agreements concluded with door-to-door salesmen within one week;
  - (c) the lack of any provision prohibiting compounded interest, i.e. the calculation of interest on interest on arrears;
  - (d) the fact that the Commission has not been precise enough about the rules which are to be laid down by the Member States to prevent a creditor repossessing the goods supplied under a credit agreement if the consumer delays payments;
  - (e) the lack of provision for licensing arrangements for lending institutions, so that disreputable operators are excluded from the outset;
6. The directive should give the consumer better protection against unsolicited visits to his home, place of work or any other place;
7. Fuller details should be given of the composition of the body to be set up to examine complaints from consumers so that consumers are guaranteed real protection;

8. The directive in question provides only minimum guarantees of consumer protection; the committees concerned therefore should adopt a position - for their respective areas of responsibility - on the limitation of credit purchasing by means of legal instruments that form part of an economic policy aimed at combatting inflation by providing greater credit facilities for transactions that may have a positive anti-inflationary influence and are therefore directed mainly at producers rather than those who want sometimes superfluous goods;

9. Article 1, paragraph 4 of the proposal for a directive should be amended to read:

"This directive shall apply mutatis mutandis to dealings between brokers and consumers".