# Putting an end to dangerous consumer credit products and irresponsible lending practices: it is time to act now.

## Introduction

Consumer credit can be a great tool-for improving the lives of millions of European citizens. It makes it possible to carry out personal and family projects that would otherwise be very difficult, if not impossible to achieve: renovating one's home, insulating it, purchasing electric cars when public transport is not easily accessible, and being able to face expenses that exceed one's monthly budget and thus spread the payment over time.

At the same time, the use of consumer credit can also turn into a headache if not a nightmare when the product is not adapted to the consumer's needs, contains hidden or excessive fees, or actively targets vulnerable consumers who will not be able to repay their loan without cutting into the family's essential expenses and basic living needs.

The consumer credit market in Europe today-presents features which are drivers of consumer harm.

- there is no EU-wide ban on usury and no capping of excessive interest rates and consumer credit costs
- creditors can grant the credit even when borrowers do not have the capacity to repay it
- the creditworthiness assessment does not consider possible negative scenarios, such as possible increases in interest rates during the contract performance
- consumers are not able to easily contest decisions based on credit scoring models and are not aware of the types of information considered to feed such models
- with digitalisation and big data, it becomes increasingly easy to exploit consumers' behavioural biases to make them sign a consumer credit contract which is not adapted to their individual and financial circumstances
- consumer credit products are increasingly complex, personalised and sold online without necessarily being adapted to the consumer's financial and personal situation

## The positive impact of a safe consumer credit market on the EU economy

The Consumer Credit Directive was last amended in 2008, in the midst of the global financial crisis. Since then, there have been many changes in the way credit market serves consumers, with new products emerging on the market and the increased digitalisation of the sector. The CCD will benefit from a necessary update and ensure that lenders act responsibly and treat consumers fairly. Responsible lending practices can lead to many positive impacts on the economy:

- **Improving access to credit and qualitative inclusion**: better risk assessment methods, based on an individual analysis of the borrowers' creditworthiness are now made available thanks to open banking and artificial intelligence (AI). If regulated property, and limited to analysing the financial and/or economic data of consumers, such methods could lead to an enlarged and more adjusted credit offer (in size/in costs) that better fits the financial capacity and needs of consumers;
- **Increasing-creditors' financial resilience** (credit institutions and other creditors) and limit risks related to the development non-performing loans (NPLs);
- **Shielding households from financial distress and over-indebtedness**, thereby limiting-social exclusion, unemployment, poverty, relationship breakdown, mental issues and an increased mortality rate which are all documented impacts of over-indebtedness.

## Improvements stemming from the European Commission's proposal

The Coalition welcomes the European Commission's proposal to revise the Consumer Credit Directive (Directive 2008/48/EC). The new proposal, published at the end of June 2021, does bring a series of positive advances related to the protection of consumers in consumer credit markets~~.~~

The revised rules significantly broaden the scope of products that will need to comply with stricter lending obligations. They will include small loans below €200, loans offered through crowd-lending platforms (online financing that connects people willing to loan money to those looking for funding) and 'buy-now-pay-later' products increasingly offered to consumers online.

The Commission also proposes to limit the sometimes-egregious costs of consumer loans, by requiring countries to cap interest rates and/or the total cost of credit. This is already common practice in several EU countries, protecting consumers from predatory loans.

## More needs to be done to achieve a resilient and safe consumer credit market

The Commission's revised proposal, although substantially improved, still suffers from shortcomings. The objective of tackling bad debt and over-indebtedness is not fully addressed: yet these challenges have been widely documented in recent years, despite the lack of sufficient statistical data.

The advances proposed do not go far enough and will not prevent the marketing of consumer credit to households that are unable to manage the repayments.

The digitalisation of financial services is still rapidly expanding, and regulation should be designed to foresee and prevent any major detriment for consumer credit users, in particular for the most vulnerable consumers in the EU.

To achieve the key objectives of limiting the risk of **irresponsible lending practices** that generate public expenditures and societal costs as well as **over-indebtedness,** the Coalition advocates for, amongst others, the following **improvements and amendments** to the European Commission's draft proposal**:**

- **Ban marketing practices (advertising and offers) which push consumers towards consumer credit products they cannot afford nor reimburse in due time.**
- **The EU should require all EU Member States to implement caps on the Annual Percentage Rate of Charge (APRC) and implement a common EU calculation method to limit the egregious costs of certain consumer loan products.** The business model of certain lenders is to charge very high interest rates for most consumers, to cover the risk of default of some. As a result, short-term high-cost loans are often extended to vulnerable consumers who cannot respect terms and conditions in a way that increases the profit of the creditors.
- **Require creditors to have product oversight and governance policies in place, and to only distribute credit products to a suitable target market.**
- **Ensure-that pre-contractual information is clear, understandable, timely, and that easy and simple consumer credit choice is facilitated.**
- **Guarantee a qualitative creditworthiness assessment** which takes into account the consumer's household budget and living expenses to limit undue exclusion
    - **Ensure that consumers** are properly informed regarding the categories of data that are used to assess their creditworthiness and ensure that they can effectively contest credit decisions, in particular when artificial intelligence is used
    - **Ensure that possible negative scenarios and changes in terms and conditions are considered at the moment of assessing the consumer's creditworthiness remain compatible with it,** including variations in interest rates

  - **Take measures to ensure that the exercise of the consumer's right of withdrawal is easy and possible in practice**, in particular when dynamic and persuasive selling techniques have been used, in linked credit agreements
- **Establish an obligation for creditors to detect financial difficulties early** and to grant appropriate forbearance measures to distressed consumer borrowers
- **Provide consumers in difficulties with immediate and personalised debt-advice solutions** to limit the risk of over-indebtedness and to allow a quick budget recovery, ensuring at all times that repayments do not impinge on reasonable living expenses, at such a level as to permit full participation of the debtor in society with dignity
- **Require the European Banking Authority to design and collect indicators to measure the quality of consumer credits market and carry out** precise NPL monitoring, including information on:
  - **Default rate by type of credit and by lender**: this ratio, which is easy to collect by national competent authorities, would make it possible to quickly identify lenders whose business model is based on a higher rate of repayment accidents
  - **Default rate and sales channel:** was the sale made by an intermediary, or online, or in a store? This information is essential for regulators to ensure that all sales methods are safe and guarantee the proper information and decision-making of both the seller and the buyer

In order to achieve the EU's climate goals and accelerate the green transition, the Coalition also advocates for the development of **standardised green loan offers (to finance energy efficient equipment & home improvements)**, setting a **stricter cap on green loans**, and **specific guarantees** to ensure that the most vulnerable consumers can also access green financing.

It is our duty, as NGOs defending the rights and interests of European citizens and consumers, to advocate for these improvements to be implemented in the revised Consumer Credit Directive.

## About the coalition

**Among the wide range of signatories of this common position, the first mentioned have developed even more detailed policy recommendations, available to anyone interested.**

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