

Proposal for a Directive of the European Parliament and of the Council on the harmonisation of the laws, regulations and administrative provisions of the Member States concerning credit for consumers

(2002/C 331 E/39)

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(Submitted by the Commission on 11 September 2002)

EXPLANATORY MEMORANDUM

1. GENERAL POINTS

1.1. Background

Directive 87/102/EEC concerning consumer credit ⁽¹⁾, amended in 1990 and 1998 ⁽²⁾, established the Community framework for consumer credit with a view to promoting the setting-up of a common market for credit and establishing minimum Community rules to protect consumers.

In 1995 the Commission presented a report on the operation of the 1987 directive ⁽³⁾, following which the Commission undertook a very broad consultation of the parties involved. In 1996 the Commission presented a report on the operation of Directive 90/88/EEC amending Directive 87/102/EEC, concerning the annual percentage rate of charge (APR) ⁽⁴⁾. In 1997 the Commission presented a summary report of reactions and comments ⁽⁵⁾.

The reports and the consultations show that there are enormous differences between the laws of the various Member States in relation to credit for natural persons in general and consumer credit in particular. Directive 87/102/EEC no longer reflects the current situation on the consumer credit market and is therefore in need of revision ⁽⁶⁾.

To this end the Commission ordered a series of studies on various specific issues ⁽⁷⁾ and carried out a detailed and comparative study of all the Member States' national transposal legislation.

⁽¹⁾ Council Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit.

⁽²⁾ Council Directive 90/88/EEC of 22 February 1990 amending Directive 87/102/EEC for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit (OJ L 61, 10.3.1990, p. 14), itself amended by Directive 98/7/EC of the European Parliament and of the Council of 16 February 1998 amending Directive 87/102/EEC for the approximation of laws, regulations and administrative provisions of the Member States concerning consumer credit (OJ L 101, 1.4.1998 p. 17).

⁽³⁾ European Commission, report on the operation of Directive 87/102/EEC, COM(95) 117 final.

⁽⁴⁾ European Commission, report on the operation of Directive 90/88/EEC, COM(96) 79 final of 12 April 1996.

⁽⁵⁾ COM(97) 465 final of 24 September 1997.

⁽⁶⁾ Communication from the Commission — Financial services: enhancing consumer confidence — follow-up to the Green Paper on 'Financial services: meeting consumers' expectations', COM(97)309 final.

⁽⁷⁾ Lea, M.J., Welter, R., Dübel, A., 'Study on the mortgage credit in the European Economic Area. Structure of the sector and application of the rules in the directives 87/102 and 90/88'. Final report on tender n° XXIV/96/U6/21 Seckelmann, R., 'Methods of calculation, in the European Economic Area, of the annual percentage rate of charge', Final Report 31 October 1995, Contract n° AO 2600/94/00101, Reifner, U., 'Harmonisation of cost elements of the annual percentage rate of charge, APR', Hamburg 1998, Project n° AO-2600/97/000169. Domont-Naert, F., et Lacoste, A.-C., 'Etude sur le problème de l'usure dans certains états membres de l'espace économique européen', Louvain-la-Neuve 1997, Contrat n° AO-2600/96/000260; Domont-Naert, F., et Dejemepe, P., 'Etude sur le rôle et les activités des intermédiaires de crédit aux consommateurs', contrat n° AO-2600/95/000254, 1996, Balate, E., et Dejemepe, P., 'Conséquences de l'inexécution des contrats de crédit à la consommation.' Etude AO-2600/95/000270 Commission européenne, rapport final.

A number of Member States have meanwhile made it known that they were also planning to revise their national legislation. This proposal for a directive is an opportunity for the Commission to anticipate these reforms and to incorporate them in a harmonised Community system.

The Commission departments concerned presented a discussion paper on 8 June 2001 setting out six guidelines for a revision of Directive 87/102/EEC and in early July 2001 they held consultations with parties representing the Member States as well as the sector and consumers. The texts proposed in this proposal for a directive take account of these consultations.

1.2. Overall assessment

Generally speaking, the first point to be made is that the concept of 'consumer credit' has undergone substantial change since the time that this legislation was initially conceived. In the 1960s and '70s we lived in a 'cash society' with credit playing a very small part and involving essentially two products, namely the 'hire-purchase' agreement or 'instalment plan' to fund the purchase of moveable property and the traditional form of credit, the personal loan. Today credit is made available to consumers via a wide range of financial instruments and it has become the lubricant of economic life. Between 50 and 65 % ⁽¹⁾ of consumers currently use consumer credit to fund the purchase of a vehicle, for example, or other goods or services and 30 % of consumers enjoy an overdraft facility on their current account. This latter credit instrument was not even in use in the 1970s to meet consumers' needs.

In macroeconomic terms the amount of credit circulating in the 15 Member States of the European Union exceeds EUR 500 000 million, corresponding to more than 7 % of GDP. The annual growth rate is overall around 7 % ⁽²⁾.

Although credit remains a driving force for economic growth and the well-being of consumers it nevertheless represents a risk for credit providers and, for a growing number of consumers, also the threat of being surcharged and suffering insolvency.

It is hardly surprising, therefore, that the Member States have found the level of protection available under the existing directives to be inadequate and have made provision in their legislation to include other types of credit and/new credit agreements which were not covered by the directives. There have also been signs that national legislation is to be amended along the same lines.

The result has been a distortion of competition between creditors in the internal market and restricted scope for consumers to obtain credit in other Member States.

Such distortions and restrictions in turn affect the volume and type of credit sought as well as the purchase of goods and services. Differences in legislation and banking/financial practices also mean that the consumer is unable to enjoy the same degree of protection in all the Member States as regards consumer credit.

Consequently, the legal framework currently in place needs to be revised so that consumers and businesses can benefit fully from the single market.

This would also be a response to concerns expressed repeatedly by consumers. The data gathered for the Eurobarometer since 1997 reveal a considerable degree of dissatisfaction with the quality of national consumer protection legislation in connection with financial services:

- more than 40 % consider that the legislation does not ensure enough transparency with regard to financial services, credit included;
- 40 % consider that the legislation does not provide adequate scope for seeking remedy against banks;
- more than 35 % consider that the legislation does not protect their rights.

⁽¹⁾ cf. Eurobarometer 54, February 2001 'Les Européens et les services financiers' and EB 56, December 2001: 'Europeans and the financial services'.

⁽²⁾ See monthly BEU bulletins.

Moreover, no less than 70 % of consumers are calling for greater, European-level harmonisation of the regulations that protect consumers.

2. SUBSIDIARITY AND PROPORTIONALITY ASSESSMENT

2.1. The aims of the directive as regards Community obligations

Various factors can explain the sluggish development of the European cross-border credit market and these include, as the main contributing factors:

- technical problems in connection with accessing another market,
- a lack of adequate harmonisation as regards national legislation,
- the changes to the methods and styles of credit that have occurred since the 1980s.

A revision of the directive calls for:

- changes to the legal framework to reflect new methods of credit,
- a realignment of the rights and obligations both of consumers and credit providers to redress the balance,
- a high degree of consumer protection.

The aim is to pave the way for a more transparent market, a more effective market and to offer such a degree of protection for consumers that the free movement of offers of credit can occur under the best possible conditions both for those who offer credit and those who require it.

To achieve these objectives the directive would need to be revised in a way that takes account of the following six guidelines:

1. a redefinition of the scope of the directive in order to ensure that it reflects the new situation on the market and is better able to draw the line between consumer credit and housing credit;
2. the inclusion of new arrangements that take account not only of creditors but also of credit intermediaries;
3. the introduction of a structured information framework for the credit provider in order to allow him to assess more fully the risks involved;
4. a specification requiring more comprehensive information for the consumer and any guarantors;
5. a fairer sharing of responsibilities between the consumer and the professional;
6. the improvement of the arrangements and practices that determine how professionals deal with payment defaults, both for the consumer and for the credit provider.

2.2. The measure falls within the Community's competence

The aim of the measure is to establish and ensure the operation of the internal market. The measure will be conducive to achieving the objective of protecting consumers by harmonising practice within the Single Market. It is for this reason that Article 95 has been selected as the measure's legal basis. As a result, the Commission's proposal is presented to the Council and to the European Parliament for adoption under the Codecision Procedure provided by Article 251 of the Treaty. Article 95 also requires the consultation of the Economic and Social Committee.

By resorting to the minimum clause provided by Article 15 of Directive 87/102/EEC and in order to protect their consumers, Member States have adopted in respect of most aspects of consumer credit provisions that are more detailed, more precise and more stringent than those contained in the directive. These differences will probably make it more difficult to conclude cross-border agreements, to the detriment of consumers and creditors alike.

The scope of the various national laws transposing Directive 87/102/EEC generally exceeds that of the directive and it also differs from one Member State to another. Legislation governing consumer credit in a number of Member States regulates leasing to private individuals with a purchase option, in other words even the lease itself for movable property held by consumers, whereas other Member States have included no such agreements in the scope of their legislation.

This means that the various styles of credit agreement calculate rates and costs in a way which differs from one style of credit to another and from one Member State to another. Directive 87/102/EEC, as amended by Directives 90/88/EEC and 98/7/EC, therefore introduced the calculation of an annual percentage rate of charge that covered all interest and costs to be borne by the consumer, allowing him more easily to compare them. However, there were two recurrent problems affecting the introduction of the APR: first, the calculation conventions for expressing both the time periods and the rounding of amounts and second, the fixing of cost — 'the cost base' — to be taken into account. To make sure that the APR is completely reliable and serviceable throughout the Community the Member States must calculate it in a uniform way and include in the same way all the cost elements linked to the credit agreement. However, despite the changes introduced by Directive 98/7/EC this is not always the case.

There are signs, for example, of difficulties with substantiating the 'obligatory' nature of insurance and sureties covering the repayment of the credit. The fact that they are obligatory means that they have to be included as costs in the cost base and this prompted a number of Member States to regulate this area beyond the requirements of the directive by use of the minimum clause. The exclusion of certain types of costs from the directive serves no (or no longer any) purpose and several Member States have therefore included these costs in their national cost bases. There are also a number of cases where the directive is not sufficiently clear, for example with regard to the effect of the commissions payable to intermediaries or taxes due when the credit agreement is concluded or performed. All of the foregoing means that there can be differences of ten, twenty or more percent depending on how strictly a Member State defines the composition of its cost base.

This proposal for a directive contains a reassessment both of the calculation conventions and of the inclusion or exclusion of certain costs on the basis of their economic justification so that a minimum of credit costs will be excluded and a maximum of clarity achieved. This should, as a rule, bring about the maximum possible harmonisation of the national cost bases and a greater degree of uniformity as regards calculation.

These measures for comparing costs are only feasible if implemented on a European scale. They will only have sufficient impact if the directive is applicable to all credit agreements offered to consumers.

Further examples can be provided: for example, the Member States' legislations use different procedures and apply different time limits for 'withdrawal', 'cooling-off' and 'cancellation' in connection with a credit agreement. These differences in terms of periods of time and procedure create obstacles for creditors who would like to offer credit in other Member States but face a waiting period of three days in Luxembourg, a period of seven days in Belgium and in the case of France they are not permitted to take any action on the credit agreement for the duration of the cooling-off period, while in other cases the credit agreement must include references to any time periods or procedures involved. The various legislations do not lay down the conditions governing the drawing up, conclusion and cancellation of credit agreements in a uniform way and distortion of competition is the result.

Some Member States absolutely forbid the door-to-door selling of credit agreements to consumers while others require a cooling-off period or even take particular steps when aggressive marketing is detected. Something that is perfectly legal in one Member State may lead to conviction in another. A creditor working in a very strictly regulated Member State could access the market more easily in another Member State that is less strictly regulated and would consequently have an advantage over his competitors.

In the event of the non-performance of a credit agreement or surety agreement a creditor will be faced with different procedures and time limits for injunctions depending on whether the consumer is a resident of one Member State or of another. The legislations of the Member States differ considerably with regard to waiting periods before any action can be taken in respect of consumers, guarantors or the repossession of goods. Longer periods and special procedures entail extra costs for creditors, who must run the risk of the agreement remaining unperformed and they may be at a disadvantage compared with a competing creditor who has no extra costs or operates in a less strictly regulated environment while all the time having granted credit to the same consumer.

Measures offering a high degree of consumer protection have been drawn up in accordance with Article 153(1)(3)(a) of the Treaty in conjunction with Article 95, as mentioned earlier. The aim of these protective measures is to strengthen the provisions put in place to establish the single market and they should enable the Member States to accept maximum harmonisation with no need for a general resort to further protective measures.

It is with this aim in view that this directive encourages recourse to out-of-court arrangements before initiating recovery procedures, the consistency of such recovery procedures with the content of the agreement, the striking of a balance between the interests both of the creditor and the consumer when payments are late, the defence of the interests of both parties when agreeing the repossession of goods financed with the credit and the possibility for the consumer to change to a different creditor, if necessary, without having to pay an unjustifiable indemnity.

2.3. The instrument most suited to the aims pursued

The measure proposed is aimed at satisfying the needs of the single market by establishing common and harmonised rules applicable to all actors — creditors, credit intermediaries etc., — thus allowing creditors to make their services more easily available and consumers to enjoy the high degree of protection.

The idea of introducing uniform legislation in the shape of a regulation that would be directly applicable under the national legislation of the Member States without transposal was studied but rejected. A directive will enable the Member States to amend the legislation in force subsequent to the transposal of Directive 87/102/EEC to the extent that is needed to ensure compliance. In drawing up its proposal for a directive the Commission has endeavoured to strike a balance reflecting the maximum possible extension of the scope of the directive to include all styles of credit and surety agreements and the desire to contain the impact of such a reform on the Member States' legislative systems. In view of the new approach to harmonisation and the many substantial changes that have been made, this new proposal will replace Directive 87/102/EEC as amended by Directives 90/88/EEC and 98/7/EEC.

2.4. Advantages of the directive being proposed

Harmonising the rules applicable to consumer credit will improve the operation and stability of European credit markets.

The proposed directive will improve the operation of the market because the scope for cross-border activities within the Single Market will be extended and competition on the market will increase. Although the rules are the same both with regard to creditors, credit intermediaries, consumers and guarantors the latter should feel more confident about credit that in some cases is unfamiliar and provided at rates or in forms that are very interesting and offered by creditors or intermediaries based in other Member States.

The directive will improve stability by putting in place a raft of provisions on responsible lending, on providing information and protection both when the credit agreement is concluded and during its performance (or in the event of its possible non-performance) that will reduce the probability of a creditor or credit intermediary being able to mislead consumers in another Member State or jeopardise their financial situation or even of acting irresponsibly. The directive being proposed, and in particular its provisions relating to the prevention of over-indebtedness, together with the rules on consulting central databases, will further improve the quality of loans and lessen the risk of consumers falling victim to disproportionate commitments that they are unable to meet, resulting in their economic exclusion and costly action on the part of Member States' social services.

3. EXAMINATION OF THE ARTICLES

Article 1 (aim)

The aim of this directive is to secure maximum harmonisation with regard to the credit on offer to consumers by guaranteeing them a high level of protection. All types and forms of credit that are available to private individuals will, in principle, be harmonised. It is for this reason that the title of the directive is worded 'credit for consumers' rather than 'consumer credit'. The few exceptions to the scope of the directive, which is very broad compared with that of Directive 87/102/EEC, are listed in Article 3.

The directive also covers surety agreements. The harmonisation being sought for these agreements will centre mainly on the information to be provided to consumers concluding such agreements, even if they guarantee credit that is granted for employment-related purposes.

Article 2 (definitions)

This article defines a number of the terms used in the directive. In principle, the terminology is identical to that of Directive 87/102/EEC. A number of changes have been introduced to cover the broader scope of the directive or to clarify some concepts. A number of new definitions have been included to cover recent additions to the text.

The definitions of 'creditor', 'consumer' and 'credit agreement' have undergone no change compared with the text of the original directive, with the exception of an improvement to the manner in which the concept of 'agreement promising to grant credit' is included. All credit transactions are covered, including promises to conclude agreements.

Credit agreements for the supply of services are also covered.

The second sentence of the definition is not intended to create an exemption. The sentence clarifies cases, such as the supply of gas water or electricity where the — continuous — supply of the services is in step with a corresponding payment but where no 'credit' is granted.

The concept of 'credit intermediary' is a general concept which could cover several types of activity and several categories of intermediary:

- an agent who is delegated and authorised to sign — exclusively — on behalf of the creditor;
- a credit broker, in other words a self-employed person working under his own name who submits credit applications to a number of different creditors;
- a 'supplier of goods or provider of services', in other words a person, (such as a salesman) who can be either a delegated agent or a credit broker, even a creditor who immediately transfers his rights to another creditor/principal funds provider who will (co)decide on the granting of credit and whose role as broker is no more than an activity supporting his principal one, namely the sale of products or services.

The definition proposed covers any person who assists in the conclusion of a credit agreement, in other words not only the credit broker but also the delegated agents or bank agents as well as the suppliers of goods and the providers of services, main or subsidiary business undertakings, including marketing assistants.

The directive thus covers any person who provides a creditor with information to identify a consumer and directs the latter, for a fee, to a creditor for the conclusion of a credit agreement. This fee may take the form of cash or some other agreed form of consideration, such as computer support, access to the creditor's business network or overdraft facilities, for example. In principle, lawyers and notaries are not covered even if a consumer approaches them for advice about the scope of a credit agreement or if they provide assistance in the drafting of an agreement or authenticate it, as long as their role is limited to providing legal advice and they do not direct their clients to particular creditors.

The 'surety' agreement covers all sureties, both personal and in material form: bonds, joint and several liability, mortgages and sureties etc. The agreement must be signed by a consumer, known as the 'guarantor' in order to distinguish him from the consumer who has concluded the credit agreement. The surety agreement may relate to any credit transaction undertaken for private or employment-related reasons provided that the guarantor is not acting in a professional capacity.

The 'total cost of credit to the consumer' must include all costs linked to the credit, including interest and other indemnities, commissions, taxes and charges of any kind that the consumer is required to pay for the credit, whether or not these costs are payable to the creditor, to the credit intermediary, to the authority responsible for levying taxes on a particular style of credit or to any other third party authorised to demand payment for services as an intermediary or in connection with the conclusion of a credit agreement or surety agreement. Although Directive 87/102/EEC already includes this interpretation, the definition has been amended slightly to clarify the inclusion of some costs but without producing a positive and exhaustive list of all cost elements.

The concepts of 'sums levied by the creditor' and 'total lending rate' are new compared with Directive 87/102/EEC and will make it possible clearly to identify the costs that are specific to the credit service offered and are payable to the creditor as distinct from all other associated charges payable to third parties, such as notary's fees, surety charges, commissions due to credit intermediaries, optional insurance charges and the like.

The borrowing rate is the interest rate used to calculate a regular payment reflecting the amount of credit drawn down and the duration of the drawdown and it excludes all other costs. An indication of this rate will enable consumers to check the interest that they are required to pay for a given period. Article 6 of Directive 87/102/EEC used the term 'annual rate of interest' but gave no other details. Some Member States opted for an annual percentage rate in conjunction with the equivalent method for conversion, where the credit was long-term credit, possibly involving a mortgage. There was a need for them to avoid the periodic rate being calculated in an infinite number of ways using different *pro rata temporis* rules that are only very vaguely linked to the linear nature of time. Other Member States permit a nominal periodic rate using a proportional conversion method. This directive seeks to make a distinction between any further regulation of the interest rates and the annual rates and indicate only the rate that is used. However, the term 'borrowing rate' has been kept in order to distinguish it from a lending rate or the rate of interest earned by savings.

The borrowing rate is thus a rate that on the basis of a particular method devised by the creditor allows the interest due on capital drawn down to be calculated periodically. This rate is different from the rate known as the 'charge' rate, that some Member States use, which is a rate calculated on the net price of goods or services to be financed but one that does not provide added value for the consumer. The annual percentage rate of charge will make it possible to pinpoint the true 'weight' of the method used to calculate this borrowing rate.

The term 'residual value' is frequently used in connection with leasing. The payment of the residual value when the option to purchase is taken up or when the credit agreement expires must enable the consumer to become the owner of the goods financed.

The expression 'credit drawdown' refers to the amount that a consumer may draw down or has drawn down as a single transaction at any given time. It represents the overall amount of credit that may be drawn down and in principle it marks the upper limit, in other words 'the total amount of credit'.

The definition of the 'durable medium' is the same as that used in the Directive of the European Parliament and of the Council of [...] on the protection of consumers in respect of distance contracts and amending Directives 97/7/EC and 98/27/EC.

The term 'third party providing constitution of capital' identifies the person other than the creditor or the consumer who undertakes in respect of the consumer, and where necessary the creditor, to constitute the capital due under the terms of a credit agreement so that the consumer is able to reimburse the creditor in accordance with the conditions of the credit agreement. This person will normally be an insurer or an investment fund.

Article 3 (scope)

This article defines the types of agreements to which the directive applies. Directive 87/102/EEC applied only to credit agreements ⁽¹⁾. It thus covered an agreement whereby a creditor grants or promises to grant to a consumer credit in the form of a deferred payment, a loan or other similar financial accommodation. This proposal for a directive is intended to extend the scope to include any guarantor, and thus any consumer, who stands surety, whether in person or in material terms and regardless of whether it covers credit granted to a consumer or to a trader. These persons must be provided with a minimum amount of information and protection similar to that enjoyed by the consumer/borrower ⁽²⁾.

The exemptions permitted by Article 2 of Directive 87/102/EEC concerning minimum and maximum amounts, free credit or credit at a reduced rate of interest, hiring agreements with an option to purchase goods or services, credit agreements in the form of an authentic act, credit in the form of advances on a current account, authorised, non-authorised or tacit overdraft as well as any other form of short-term credit involving charges or interest to the consumer need to be removed. ⁽³⁾

There is, however, a case for exempting credit agreements, the purpose of which is to grant credit for the purchase or transformation of a private immovable property as covered by a Commission recommendation. However, the directive will apply to such credit agreements if their purpose is to finance, possibly by means of a new drawdown of credit, transactions other than the purchase or transformation of private immovable property.

There should also be exemptions in respect of agreements with provision for deferred payment or similar financial accommodation, possibly involving the use of a payment or debit card, where such transactions are free of charge and completed within three months.

⁽¹⁾ Court of Justice. Judgment of 23 March 2000, Case C-208/98, Berliner Kindl Brauerei AG.

⁽²⁾ Similar or comparable legislation in the MS — non-exhaustive list for F, UK, L, B, IRL, and S.

⁽³⁾ The Member States have comprehensively stretched the limit of scope of Directive 87/102/EEC. Similar or comparable legislation in the Member States — a non-exhaustive list grouped by exemption: Art. 2(1)(a) IRL, F (in part), NL, A. (moreover, several MS, including Belgium, have clear cut protective legislation); Art. 2(1)(b) IRL, F, L, UK, B, NL; Art. 2(1)(c) DK, NL, F, IRL, B; Art. 2(1)(d) DK, NL, F, IRL, B; Art. 2(1)(e) D, F, P, B, DK, A, UK; Art. 2(1)(f) D, A, DK, IRL no upper limit; B and S very fragmentary upper limit, F and NL fragmentary upper limit, L and UK higher upper limit IRL, F, NL no lower limit, S and B fragmentary lower limit, L lower minimum; Art. 2(1)(g) B, F, IRL, L, NL; Art. 2(2) Exception cited only by IRL, UK (Credit Unions), NL, B (social loans), and D (credit from employers). New text covers NL, B and D; Art. 2(3) A, IRL, in part NL and L; Art. 2(4) Exclusion linked to and to be compared with 2,1, a).

This directive is not intended to cover situations where an employer occasionally, and not as part of his or her main business or professional activities, grants credit or an advance on his or her salary to a member of his or her staff. However, there is no case for allowing Member States to exempt from the scope of this directive certain forms of credit that are made available to particular groups of people or at a reduced rate of interest under special circumstances, where such credit is offered systematically as part of business or professional activities either to members of a cooperative created specifically for the purpose or whenever an employer sets up a 'credit' facility within his or her undertaking. In such cases the credit must be granted with the same degree of caution as that required under this directive and be accompanied by the same amount of information, advice and measures aimed at protecting consumers.

Lastly, there is a case for exempting credit agreements concluded between investment firms such as those referred to in Article 1(2) of Directive 93/22/EEC and investors ⁽¹⁾. Such agreements cover credit of a very specific type to which similar provisions apply, in particular as regards information and advice.

Article 4 (advertising)

Article 3 of Directive 87/102/EEC states that: 'any advertisement, or any offer which is displayed at business premises, in which a person offers credit or offers to arrange a credit agreement and in which a rate of interest or any figures relating to the cost of the credit are indicated, shall also include a statement of the annual percentage rate of charge, by means of a representative example if no other means is practicable'. The purpose here was to avoid unfair or misleading advertising based on the display of a rate of interest or of a cost without the consumer being advised of the real cost of, or rate for, the credit agreement.

The wording of Articles 1(a)(3) and (3) shows that from the outset the Member States were in doubt as to the scope and methods for calculating the annual percentage rate of charge (APR). A number of derogations were therefore accepted that would allow the reference to the APR to be replaced by an approximate method using a representative example wherever it was impossible to state the APR in clear and simple terms without, however, explaining either the exact circumstances under which the representative example was to be used or how it was made up. It was, in fact, always possible to calculate an APR but this involved using the assumptions listed in Article 1(2)(7) of Directive 87/102/EEC as replaced by Article 12 of this proposal for a directive.

The advantage of a reference to the APR compared with a separate reference to the various cost elements — annual or periodical — is that the APR takes account of the 'periods' at which the creditor requires payment. The APR is thus the prime indicator par excellence of the weight of the cost to be met during a given period in connection with the repayment of any kind of credit agreement. However, it was not always clear beforehand in connection with advertising what the frequency of drawdown and/or repayment would be and this explains the need for the use of assumptions. It is possible, however, that in certain circumstances, such as the case of advances on current accounts, that three or four assumptions might be applicable at the same time: immediate drawdown, repayment after one year, fixed rate for a given period. Imposing a requirement that similar information in a representative example should be made available via audiovisual advertising could be seen as disproportionate and the prohibiting of any reference to cost or rate in the cases covered by Article 3 appears equally inconceivable.

The most flexible solution proposed in Article 4 of this proposal for a directive is to include a reference to the provisions of Directive 84/450/EEC of 10 September 1984 concerning misleading and comparative advertising. An assessment of the misleading content will depend on the type of credit agreement and on the factual information accompanying the advertising.

⁽¹⁾ OJ L 141, 11.6.1993, p. 27.

Article 5 (ban on negotiation of credit and surety agreements outside business premises)

A number of Member States ⁽¹⁾ found the active door-to-door selling of credit agreements unthinkable in a normal commercial relationship between a creditor or credit intermediary and a consumer, in particular given the impact of door-to-door selling on consumers' commitments. Door-to-door selling of credit agreements may have particularly serious consequences for consumers who, in the situation referred to in Directive 85/577/EEC ⁽²⁾ and in spite of the protection afforded by the said directive, are unable to assess the full financial impact of any credit agreement that is concluded. The impact will not be felt until the first repayment is made. In view of the specific nature of the credit and the attendant financial consequences it has been deemed necessary to adopt a stricter approach than that required by Directive 85/577/EEC and to ban any unsolicited door-to-door selling of credit of the type to which this directive refers. It is therefore proposed that there should be a ban on credit agreements and surety agreements concluded under circumstances that are similar to those for agreements described in Article 1 of the said directive with provision for the fact that the term 'trader' can relate both to a creditor and to a credit intermediary.

Article 6 (exchange of information in advance and duty to provide advice)

This article regulates the information to be provided for consumers in advance and the duty on the part of the creditor or credit intermediary to provide advice ⁽³⁾.

The creditor and, where appropriate, the credit intermediary may only ask information of the consumer or guarantor that under the terms of Article 6 of the directive is appropriate, relevant and does not exceed that which is required for the purpose for which the information is collected and processed. The consumer and the guarantor are required to answer sincerely the precise questions put by the creditor and, where appropriate, the credit intermediary.

Before the credit agreement is concluded the consumer must be provided with enough information about the cost of the credit and his obligations. The rules proposed mainly reflect that which was stipulated concerning information in advance in the Commission's recommendation of 1 March 2001 on pre-contractual information to be given to consumers by creditors offering home loans ⁽⁴⁾. The information must therefore cover all aspects of the credit agreement (whether it is a fixed-rate or variable-rate credit agreement, what conditions govern variations in the rate, drawdown, repayment etc.) and some of this information must constitute the compulsory information to be included in the credit agreement. As regards distance contracts the preliminary information must be provided in a way that is consistent with the requirements of Article 5 of Directive ... of the European Parliament and of the Council on the distance marketing of consumer financial services and amending Council Directives 90/619/EEC, 97/7/EC and 98/27/EC.

The tailored information must include a reference to the annual percentage rate of charge. The APR mentioned in the said information must be the same as the final APR shown in the credit agreement unless it is based on contractual elements that are unknown when the information is provided. The consumer should at least know that assumptions have been used and what they are so that he can be notified and is able to check the components of the APR and, by extension, of the credit being offered: amounts to be drawn down, amounts to be repaid and the periods. The same argument must apply to the total lending rate. Any reference to a rate or a cost that does not feature in any such assumption is considered to be misleading. It is with this aim in view that for distance credit agreements the preliminary information is given over the voice telephone as referred to in Article 3(3) of Directive ... must include the APR and the total lending rate as well as their respective components.

⁽¹⁾ Similar or comparable legislation in the MS — non-exhaustive list: UK, B and L; partial legislation in respect of certain effects or door-to-door selling situations: IRL and NL.

⁽²⁾ See Court of Justice. Judgment of 13 December 2001, Case C-481/99.

⁽³⁾ Similar or comparable legislation in the MS — non-exhaustive list: paragraph 1 and paragraph 2: most of the MS, for example, F and B: offer in advance, NL: prospectus; IRL and L: information relating to advertising, the activities pursued by the credit provider, UK: the duty to provide information and to specify this information for each credit agreement etc. paragraph 3: B

⁽⁴⁾ JO L 69, 10.3.2001, p. 25.

The use of assumptions is limited. Article 1(a)(7) of Directive 87/102/EEC already imposed strict conditions which have been incorporated into this proposal for a directive. Replacing the timetable by the assumed full repayment after one year, for example, is only possible if the said timetable is not shown in the text of the agreement or is not evident from the means by which the credit granted is to be paid.

As regards the creditor and, where appropriate, the credit intermediary, there is a need to ensure that they have a general duty to provide advice so that the consumer can choose the best type of credit from the range normally offered by the latter. This advice must take account of the consumer's ability to repay, the risk entailed, the existence or not of a fixed timetable, the scope for drawing down the credit and the purpose for which the credit sought is to be used.

Article 28 of the directive regulates the status of credit intermediaries who, without being registered, work for a licensed creditor or a credit intermediary who assumes responsibility for them. Here, the credit intermediary must provide the information and advice but responsibility is assumed by the licensed creditor or credit intermediary. Article 6(4) regulates the case where a credit intermediary is a supplier of goods or a provider of services that are only subsidiary in terms of their impact on the procedure for offering and concluding the credit agreement. The duty to provide information and advice is thus fully that of the creditor or the credit intermediary for whom this supplier acts when concluding credit agreements, possibly acting as a marketing assistant.

Article 7 (collection and processing of data)

Highly personal information that the consumer or the guarantor provides in connection with the conclusion, management or performance of a credit agreement or surety agreement is frequently collected for the purpose of processing it for applications other than risk assessment: advertising, marketing, offers of insurance contracts, marketing and sales of such data to third parties etc. The consumer's agreement is often obtained using the credit application form or a clause featuring in the credit or surety agreement that under certain circumstances do not allow the consumer really to refuse in view of the risk he would run in having the credit or the financial accommodation withheld. In most cases the consumer is even unaware that he has put his signature to such a clause.

This article authorises the collection and, *a fortiori*, the processing of this information by persons acting in the transactions covered by this directive only in order to assess the financial circumstances of the consumer or of any guarantor and of their ability to repay. It is, in other words, a formal obligation that rules out any purpose linked to marketing or the sale of personal data collected under the terms of this directive. The directive must offer an assurance that the obligation, referred to in Article 6, namely without prejudice to the application of Directive 95/46/EC, to provide data that in some cases are highly personal and sensitive, to the creditor and the credit intermediary is complied with. However, this clearly defined objective applies equally to information collected during the management of the credit or surety agreement and this includes non-performance. The persons concerned are therefore not only creditors and credit intermediaries but also information bureaux as well as credit insurers whom the creditor contacts in his information search in accordance with Article 9. The list could be extended to include debt recovery agencies and in general any person who takes over the debt owed to the creditor.

Article 8 (central database)

The avoidance of overin-debtedness, both on the part of the consumer and of the guarantor, is a matter of general interest. The setting-up of centralised databases can to an extent solve this problem and at the same time the creditor could be made responsible by the imposition of civil and trade sanctions if on the basis of the information he obtained he ought to have decided not to grant new credit. The Member States ⁽¹⁾ should make it compulsory to maintain a central database holding negative, neutral and reliable data recording late payments, containing identification of consumers and guarantors and covering at least the territory of the Member State in question with guaranteed access to all creditors.

⁽¹⁾ Similar or comparable legislation in the MS — non-exhaustive list: the situation differs widely from one MS to another: NL and B: virtually similar legislation but extended to include positive files, D, A and I: positive files that go beyond the positive recording of data on credit and surety agreements with no consultation requirement; F and DK: only negative files with no consultation requirement. By way of contrast, UK: no central database, virtually unrestricted freedom to set up private decentralised databases with no common criteria or consultation requirement.

Article 8 makes the existence of such a database compulsory and introduces a common platform for accessing, processing and consulting the data.

The final paragraph in Article 8 has provision for the Member States to go further by setting up central positive databases recording all consumer commitments relating to credit. The creditor would thus have at his disposal an instrument that is more reliable than a negative database and which would offer him scope for checking whether a consumer, or possibly a guarantor, had concluded other credit or surety agreements that have not been the subject of litigation but where the associated total financial burden rules out the receipt of any further credit.

The concept of 'responsible lending' as it appears in Article 9, obliges the creditor to consult the central database before the consumer can conclude a credit agreement or a guarantor has undertaken to guarantee repayment of the credit in question. Clearly, consulting this central database is for the creditor no more than an initial and helpful indication that must be backed up by other measures, as described in Article 9. Nevertheless it is considered appropriate that for the sake of transparency the creditor should inform the consumer, at his behest, of the results of this consultation of the centralised data base. This information must enable the consumer and the guarantor, if necessary, to require the controller of the file to carry out any corrections that are necessary.

The database may only be consulted on a case-by-case basis. The data released by the database may be used only for assessing the risk of non-performance of the credit or surety agreement and any marketing or sales application is prohibited. The personal data may be held only for the time needed to assess the risk and must be then immediately destroyed once the credit or surety agreement has been completed or the credit application turned down. The controller of the file at the central database may, however, retain a record of the consultation and if required may make it available to the person concerned in court if, for example, the responsibility of the creditor were to be called into question or contested under the provisions governing 'responsible lending'.

Article 9 (responsible lending)

Some Member States ⁽¹⁾ have a number of rules in connection with credit requiring creditors to apply caution or to act as 'good creditors'. This article is intended to establish a similar principle on a European scale, not only in the interests of all consumers or guarantors but also of all creditors. The latter are at risk of seeing their clients' solvency diminished because their competitors subsequently conclude credit agreements under circumstances that seriously jeopardise the consumer's or the guarantor's ability to repay.

The principle of 'responsible lending' represents an obligation to consult centralised databases and to examine the replies provided by the consumer or the guarantor, to request the provision of sureties, to check the data supplied by credit intermediaries and to select the type of credit to be offered. It is not an obligation targeted at obtaining results such as the existence or otherwise of fault on the part of the consumer. Similar rules requiring caution call, moreover, for an assessment of the facts and for an examination on a case-by-case basis, preferably by the legal authorities. Any assessment by the creditor of a consumer's ability to repay is, however, in no way impartial: he is contractually bound and it is matter of some importance that the link should be made clear between the conclusion of the credit agreement and the preliminary assessment.

This provision is without prejudice to the obligation on the consumer to act with prudence when he looks for credit and to respect his contractual obligations.

Article 10 (information that must be included in credit and surety agreements)

As regards the information that must appear in the credit agreement, Article 4(2) of Directive 87/102/EEC indicates that only a minimum of information is to appear. The third paragraph of this Article makes a reference to the Directive's Annex I that lists the 'essential' conditions which the Member States *may* require to be mentioned in the written agreement. Almost all the Member States have therefore regulated the form and content of credit agreements in a general manner and other specific credit agreements in a variety of ways.

⁽¹⁾ Similar or comparable legislation in MS — non-exhaustive list: NL, B and for guarantors F and S.

The first paragraph of Article 10 contains a paragraph common to credit agreements and surety agreements alike. All the parties must receive a copy of the credit agreement, including the credit intermediary who, strictly speaking, is not a 'party', but who needs to be kept informed, in particular regarding the payment of his salary. Both the credit agreement and the surety agreement must contain an indication of any extrajudiciary procedures that might apply.

Article 10 of this directive proposes that there should be a complete and compulsory list of information, essentially the information referred to in Article 6. If a minimum of compulsory information in the credit agreement is required, there is also a need for this information to be relevant, legible and accurate and for it to be consistent with the information that was provided prior to the conclusion of the credit agreement. The general conditions, in particular those governing the operation of an account or that regulate a variable rate of interest, form an integral part of the credit agreement.

The total amount of credit must always be shown (since no creditor grants limitless credit) and this amount cannot be changed without a new agreement (novation). The words 'if any' appearing in the Annex to Article 4 of Directive 87/102/EEC have therefore to be deleted. Some creditors set intermediate upper limits and raise (or lower) these upper or lower limits unilaterally depending, *inter alia*, on whether the consumer makes regular repayments or not, whether or not he uses his credit line, whether the credit is profitable or not or whether the national maximum rates have changed.

If one of the parties seeks to increase the total amount of credit (i.e. raise the upper limit), he must request a new contract and the creditor is obliged to carry out a new solvency check (which implies that 'intermediate upper limits' are not, or no longer, permitted).

The reference to the 'amount drawn down' in the credit agreement is pointless and has been removed. On the other hand, additional information relating to Article 6 of this proposal for a directive is required and this information should include the amortisation table, a reference to the object being financed in the case of an 'assigned credit', any cash downpayment required if it relates to hire purchase and the rates and charges applicable should the credit agreement not be performed.

Surety agreements must also contain a minimum amount of data, namely a reference to the 'amount guaranteed' and the charges associated with the non-performance of the surety agreement that are quite separate from those of the credit agreement. Charges associated with the conclusion of the surety agreement are in practice payable by the consumer and should therefore be included in the annual percentage rate of charge. Even if the guarantor were required to pay them himself he would under national law in all the Member States be entitled to seek remedy against the consumer, which means that the payment of any such debt should also be included in the total cost of the credit.

Article 11 (right of withdrawal)

The cooling-off period and the option to withdraw are well-established traditions ⁽¹⁾ by means of which the consumer may release himself from an ill-considered commitment and change a decision taken at a time when the pressure applied by the salesman outweighed the consumer's free and enlightened will to choose. This article proposes there should be the option of withdrawal under circumstances similar to those referred to in the Directive of the European Parliament and of the Council [...] on the distance marketing of consumer financial services and amending Council Directives 90/619/EEC, 97/7/EC and 98/27/EC. The Commission has selected this approach in order to harmonise the procedures for exercising the right to withdrawal in similar situations. The Commission is aware of existing differences in other directives on consumers' rights. As it reported in its Strategy for Consumers 2002-2006 the Commission is planning a revision of the matter to follow up its Communication on European Contract Law.

⁽¹⁾ Almost all the MS have something similar. Similar or comparable legislation in the MS — non-exhaustive list: B: right of 'renonciation' during a period of seven working days, R: 'rétractation' period lasting seven days, IRL right to 'withdraw' for 10 calendar days, L: right 'à se départir' but only for credit agreements granted by a supplier and within two days. UK: 'cooling-off period' various arrangements, D and A: 'Widerrufsrecht'.

The article is not an obstacle to the immediate drawing-down of credit. The creditor may in this instance require a consumer who is exercising his right to withdrawal to pay a maximum indemnity that is consistent with the amount obtained by applying the annual percentage rate of charge to the amount drawn down with effect from the date of drawdown and up until such time as the APR ceases to apply following the repayment of the funds or the return of the goods. Any such indemnity would be very small in the case of small amounts of credit but it should at least help to stem abuse and speculation in the case of larger amounts. Moreover, the consumer will be required to return the goods that he obtained in connection with the credit agreement to the creditor whenever the credit agreement stipulates that the goods are to be returned. Where there is a legal difference between a credit agreement and a purchase agreement the consumer will be required to honour the purchase agreement unless it was concluded as a resolute condition linked to the conclusion of the credit agreement.

Article 12 (annual percentage rate of charge)

Article 12 shows how the annual percentage rate of charge is calculated. It replaces and extends Article 1(a) of Directive 87/102/EEC as inserted by Directive 90/88/EEC.

The formula for the annual percentage rate of charge, to which reference is made in Annex 1, is retained with the exception that different terminology is used to reflect the new definitions appearing in the proposal for a directive. The proposal is for complete standardisation in respect of rounding-off and what is understood by a year. Only the method for calculating fractions of a year has been retained. Annex 2 shows a number of examples of calculations that cover all types of credit agreement.

The total cost of the credit must include all costs, including borrowing rate plus all the other indemnities, commissions, taxes and charges of any kind that the consumer is required to pay for the credit regardless of whether these costs are payable to the creditor, to the credit intermediary, to the competent authority levying the taxes or to any other third party authorised to receive payments following the brokering or conclusion of a credit agreement or surety agreement.

Directive 90/88/EEC established two exemptions and these have been retained in paragraph 2: the charges for non-performance and the charges payable in cash or by credit. Clarification is provided regarding some 'media' associated with the credit agreement: cards and accounts. Charges linked to these media must be included in the total cost of the credit and thus also in the APR unless the creditor has clearly and distinctly defined in connection with these media the costs that are linked to credit transactions and the costs that are linked to other payment transactions.

Clearly, any insurance guaranteeing repayment of the credit reduces the level of risk to which the creditor is exposed and the premium in such cases must be viewed as a constituent element of the cost of the credit. This principle has been kept for certain types of insurance in exemption (v) of Article 1(a) of Directive 87/102/EEC. Some Member States ⁽¹⁾ have broadened the 'freedom of choice' aspect to include other types of insurance and have widened the concept of 'total cost of the credit' to include any compulsory insurance, the premium for which must be included in the calculation of the APR. These countries have noted that there was in practice no freedom of choice for consumers and that the creditor, acting with circumspection or with a view to his profits, preferred to negotiate — automatically — insurance cover even if the consumer had not initially asked for such insurance. The Member States also had problems proving the 'compulsory' aspect of the insurance and sureties covering repayment of the credit as the compulsory nature of such was the condition governing their inclusion as cost elements in the base. This proposal for a directive aims to end this discussion by proposing to include automatically any insurance premium in the total cost of the credit, provided that the insurance is taken out at the time that the credit agreement is concluded.

⁽¹⁾ Similar or comparable legislation in the MS with regulations that in general terms exceed the directive by guaranteeing a fuller base: B, E, F, NL, A, S; MS with unique solutions or which include the insurance charges: B, DK, E, F, NL, A, S, UK.

On the other hand, the gains resulting from insurance covering death, invalidity, sickness and unemployment, namely the amount corresponding to early repayment of the capital and early repayment indemnity or the commitment fee, are not to be included in the APR. The payment of these amounts is not agreed on an exact date shown in the credit agreement and the consumer, in point of fact, has no plans to effect such transactions.

However, the gains from life assurance covering reconstitution of the capital when the credit agreement comes to term amounts to an obligation within a period and on an agreed date even if the conditions are described in an additional agreement annexed to the credit agreement.

Whenever necessary, a number of the assumptions referred to in paragraphs 3, 4 and 5 should be used to calculate the annual percentage rate of charge. The consumer should be notified of these assumptions every time that a calculation is carried out that is based on them. They may only be used if the constituents of the calculation in question are not known at the time of the advertising, at the time the information is provided or are not evident from clauses in the agreement or from the means of payment used to access the credit granted.

The assumption based on the absence of any credit limits, as shown in the first indent of Article 1(a)(7) of Directive 87/102/EEC has been abandoned. This proposal for a directive provides for a total amount of credit always remaining and being mentioned. However, an assumption has been included in respect of credit drawdowns. Where a consumer may draw down credit at any time and in any amount — but within the limits imposed by the credit agreement — the creditor would be unable, when calculating the APR, to include such aspects in advance. He must therefore presume that the whole amount of credit has been drawn down immediately so that a credit agreement of this type can be compared to a traditional loan.

Paragraph 6 regulates the special case of leasing. Credit agreements of this type generally have provision for parameters on which the residual value of the goods financed can be determined, this residual value being payable when the consumer opts to purchase the goods. In this case, either the credit agreement has an arrangement whereby this amount can be calculated in advance down to the last euro-cent, and these figures are used to calculate the annual percentage rate of charge, or else the contract includes parameters that do not allow an ex-post calculation and, accordingly, the assumption of the linear amortisation of the goods applies.

Lastly, Annex III shows a formula and some examples for working out the impact of compulsory, front-end saving on the annual percentage rate of charge.

Article 13 (total lending rate)

The total lending rate is a rate showing what is payable to the creditor for his 'credit service' and it excludes all charges payable to third parties. It is calculated in the same way as the APR and its one base reflects only the costs payable to the creditor. These costs include the interest payable, administration and management charges, credit insurance premiums, and in general terms the insurance premiums payable by the consumer upon conclusion of a credit agreement provided that it is the creditor who stipulates the insurance requirement and chooses the insurer. In other words the premium is not a component of the base if the insurance — like all other associated services — is optional. All charges relating to sureties, notaries' services, taxes and registration fees and the like are similarly not taken into account for the purpose of establishing the total lending rate.

Article 14 (borrowing rate)

Article 2(k) has defined the concept of borrowing rate as an interest rate that excludes all other costs. This proposal for a directive essentially lays down rules governing how the borrowing rate may vary. The periods during which the borrowing rate may vary must be indicated in the credit agreement. Indices or reference rates may be chosen freely on condition that they are governed by objective rules that are clear and cannot be influenced by what the parties prefer.

It is only this rate that may be varied. No other charge may be varied and it is unthinkable that 'costs' may vary. It would be very difficult to allow the costs associated with the conclusion or the management of a credit agreement (commissions, stamp duty, postal charges etc.) to vary, either downwards or upwards. It is, in fact, only the cost of money that can vary over time. It is for this reason that the charge rate cannot be allowed to vary. The price of goods or of a service is fixed in advance and payments are staggered over time. The possible cost of refinancing this transaction by the creditor is already included in the rate of charge and is therefore, by its very nature, not subject to variations of any kind.

The consumer must be advised of any change to this rate, for example by providing a statement of account. A reference to a new annual percentage rate of charge will allow the consumer to know whether his credit, following application of the rules governing variations in rates, has not become too expensive compared with the market rate.

Article 15 (unfair terms)

The list of unfair terms contained in this article should be seen as a 'black list' of specific clauses that should not appear in any credit or surety agreement. It should not be understood as a special list to replace the (grey) list or the general clause in Directive 93/13/EEC on unfair terms. It is for this reason that there is a mention to the effect that the article applies 'without prejudice to the application of Directive 93/13/EEC to the agreement as a whole'.

The ban referred to in point (a) covers practices that require or reserve some part of the sums borrowed, for example, to constitute a surety, deposit or bond, or to purchase shares in a bonding company or a financing company, as these are practices that would double the profits of the creditor or, where applicable, the credit intermediary.

The provision of point (b) is to regulate the joint offer of a credit agreement and another agreement that most frequently relates to the provision of some ancillary service — insurance, maintenance, current account, etc. without the consumer being given the choice of declining the service or selecting a different provider. Where there is no freedom of choice the related charges must form part of the total cost of the credit.

The provision of point (c) requires any change to the APR to apply only to variations in the borrowing rate and to no other charges. It is difficult to imagine costs relating to stamps, customer records, account statements and management etc. being subject to rules on variability. For any unilateral raising of costs a new credit agreement must be drawn up.

The provision of point (d) relates to a ban on any condition permitting disproportionate variability vis-à-vis the consumer where such a condition uses, for example, different calculations depending on whether the rate rises or falls, uses rates or indices for variability that are not quite neutral or even depend on the creditor's personal preferences etc.

The ban referred to in point (e) relates to a practice that takes the form of applying initially a call-in rate or a discounted rate that are then followed by a cost base that is higher and subject to the rules on variability. The rate advertised must be the cost base and any discount must be advised separately.

The provision of point (f) relates to agreements known as 'balloon agreements'. It has been noted that this type of 'timetable', the last payment under which — the residual value — is fairly high, is made available by captive companies, the purpose of whose trade is to retain consumers for their particular make of car. These agreements frequently involve refinancing or a return of the object financed as a deposit for a second purchase of a car that includes a new credit agreement. Such business practice appears questionable in that it is likely to prevent consumers changing the make of car owing to the final financial burden involved.

Article 16 (early repayment)

Article 8 of Directive 87/102/EEC grants the consumer the right 'to discharge his obligations under a credit agreement before the time fixed by the agreement'. This right was amended and the article then read as follows: 'in this event, in accordance with the rules laid down by the Member States, the consumer shall be entitled to an equitable reduction in the total cost of the credit'. Accordingly, the creditor is also entitled to require an early repayment indemnity — a fair one — to offset his charges and lost investment.

A number of Member States have specified, even banned, this indemnity⁽¹⁾. It is difficult nowadays, given the scope for reinvesting capital on the international capital market, to justify any indemnity or financial compensation. The proposal is therefore first and foremost to confirm the right to early repayment, either in part or in full.

By seeking to strike a balance between the advantages for the consumer and the disadvantages for the creditor — relating to the management of the early repayment and the reinvestment of the capital received — the proposal is therefore to include provision for an early repayment indemnity for creditors only if it is objective, fair and calculated on the basis of actuarial principles. In other words, the method used must be objective and must pinpoint cases where an indemnity is not called for, for example when market rates are on the rise, which would make the indemnity negative and in fact offer a profit to the consumer. The principle of 'actuarial fairness' is fully respected so that the points of view of both parties can be given the best possible consideration.

The proposal is nonetheless to exempt the consumer from the payment of an indemnity for any credit agreement whose conditions do not justify an indemnity:

- point (a) is therefore aimed at excluding credits at variable borrowing rates where the cost of early repayment is largely passed on through the rate. However, the variable rate must apply to periods of less than one year.
- point (b) excludes credits covered by insurance. None of the parties concerned is interested in maintaining the credit — quite the contrary, for the sums paid under the terms of an insurance agreement should allow the contractual relationship to be terminated.
- point (c) concerns credits without capital amortisation, such as advances on current accounts, and in general any form of credit where the interest is calculated *ex post* to reflect the duration of the drawdowns that occurred. The absence of any obligation to repay 'in instalments' or by periods means, moreover, that there is no 'early' repayment. Credit agreements with provision for constitution of capital, to which Article 20 refers, are not covered by point (c) because they have special procedural methods for repayment at the end of periods and special conditions apply to the calculation of interest.

Article 17 (assignment of rights)

This article corresponds to Article 9 of Directive 87/102/EEC. The wording was changed only to incorporate new definitions and enhanced protection for the guarantor. An assignee is understood as any person to whom the creditor's rights have been assigned, in other words a credit insurer, debt collection agency, a rediscounting company or securitisation company etc. without reference having been made to the legal procedure followed — assignment of credit, subrogation, delegation etc.

Article 18 (ban on the use of bills of exchange and other securities)

This article replaces Article 10 of Directive 87/102/EEC and completely abandons the use of bills of exchange, promissory notes or cheques as a means of payment and/or form of personal surety.

⁽¹⁾ Similar or comparable legislation in the MS — non-exhaustive list: (1) with restrictions regarding the calculation and/or the amount of the indemnity: IRL, NL, B, L, UK, (2) with ban: F

Article 19 (joint and several liability)

This article replaces Article 11 of Directive 87/102/EEC. Article 11 was based on the concept of joint and several liability under common law, i.e. the responsibility of a number of people who, in law, are held jointly and severally responsible for the discharge of an obligation. The wording ultimately used for Directive 87/102/EEC, termed 'subsidiary responsibility', is a compromise with provision for the 'consumer' under certain circumstances being able to claim payment from the creditor if his complaint against the vendor is justified and the latter refuses to pay. A number of Member States simply transposed Article 11 and created legislation that was ineffective. Other Member States went beyond the requirements of the provision and deleted the concept of 'exclusive link' in relations between the creditor and the supplier or provider ⁽¹⁾.

The consumer needs to be given a right to act directly against the creditor when the creditor enjoys trade benefits by working with specific suppliers and is able to seek remedy against them. Whenever the creditor has close trade links with the supplier of the goods or the provider of the service the damage, in the event that the consumer receives only faulty goods or services, or only some of the goods or services he ordered or even receives none at all, should not be borne by the consumer but by the creditor or the supplier. The consumer should have the option of going to court against one or the other or both in order to recover the amount of his damage.

The proposal is therefore to adopt comprehensively the joint and several liability solution when the credit supplier and the supplier of the goods or services are joint market operators. A case in question would therefore be where the supplier has acted, even in an ancillary capacity, as a credit intermediary. An existing agreement and effective checks by the creditor can be taken for granted in such cases and the consumer should not be required to provide proof. This possibility covers not only the credit that has been assigned in the strict sense but also any other form of credit availability or debit account that the supplier proposes to the consumer on the occasion of the first purchase. It will be remembered in this respect that this proposal for a directive contains a provision requiring the identity of the intermediary to be shown in the credit agreement.

Article 20 (credit agreement providing constitution of capital)

For some years now the range of credit available has been growing to include new mortgage-linked credit tied to either life assurance or to investment funds, the latter being generally known, in the UK, as endowment mortgages. Up until quite recently only traditional life assurance was used for the constitution of credit. However, the new method, which uses a fund, is not without its risks for consumers. As in the case of variable-capital investment companies or shareholdings, the sums constituted are dependent on how the financial markets behave. It is possible, therefore, that when the main credit agreement comes to term there is not enough capital to repay the credit, something that is not permissible in connection with a product that is offered to the general public. Moreover, a similar situation has arisen on the UK market with the result that consumers have encountered difficulties with repayments. It is therefore appropriate that where there is no constitution of capital the creditor should assume one way or another responsibility for its repayment, possibly using an additional insurance for this purpose. Paragraphs 1 and 2 are intended to regulate such situations.

Paragraph 3 sets out special rules governing the calculation of the APR and the total lending rate that include all payments to be made by the consumer both in respect of the main credit agreement and the additional contract covering the reconstitution of capital.

⁽¹⁾ Similar or comparable legislation in the MS — non-exhaustive list: in the UK there is a system of 'pure' joint and several liability without any exclusive link but which has now a lower and an upper limit. Other MS such as F and D have developed 'independent' systems. The B, IRL, F and L have not kept a lower limit. NL has a lower limit.

Article 21 (credit agreement in the form of an advance on a current account or a debit account)

This article proposes the establishment of a standard method for providing information during the term of the credit agreement so that the consumer is able to check the accuracy of the credit drawdowns that have occurred, the borrowing rate applied, the costs to be paid etc., in particular in connection with credit agreements linked to the operation of an account for which the borrowing rates are calculated ex post.

Article 22 (open-end credit agreement)

This article proposes that the consumer — and the creditor — should be entitled to terminate an open-end credit agreement by giving three months' notice. It is felt that a period of three months is the minimum period for the consumer, who must be able to repay the total amount of credit he drew down. The consumer retains the right to seek damages and interest if such termination by the creditor is to the prejudice of the consumer.

Article 23 (performance of a surety agreement)

The first paragraph prohibits surety agreements that relate to open-end credit agreements. A guarantor frequently only has a brief look at a consumer's solvency. Requiring a guarantor to provide a 'lifelong' surety must be considered excessive from the point of view of his own interests and may risk leading him into debt.

The second and third paragraphs place restrictions on the action that can be taken against the guarantor. The provisions of this directive place the emphasis on risk assessment relating to the consumer whereas the guarantor's solvency and risk assessment in his case are of no more than secondary importance.

The proposal is therefore that the creditor may not approach the guarantor until a period of 'insolvency' has passed. The creditor must alert the guarantor — in good time — if the consumer is defaulting on payments so that the guarantor can, if necessary, take steps to ensure that the consumer's indebtedness does not deteriorate further.

Lastly, the proposal is that the amount guaranteed by the surety may relate only to the outstanding balance of the total amount of credit owed by the consumer and to any arrears or possible charges with the exclusion of any form of penalty or non-performance indemnities payable by the consumer. These indemnities, that in principle are the consumer's responsibility, may be limited to this amount on condition that the guarantor immediately meets his obligations. It would indeed be unfair if the guarantor were required to pay additional penalties owing to the consumer's inability to discharge his obligations. If, on the other hand, the guarantor were late in meeting his own obligations the creditor could seek arrears and additional penalties in line with the amount that was guaranteed but not paid.

Article 24 (default notice and enforceability)

Paragraph 1(a) of this article should be seen as the principal element linking all the articles in this chapter covering the non-performance of credit agreements. It establishes a general principle of proportionality in respect of the recovery of debts arising out of a credit agreement or surety agreement.

The aim of Paragraph 1(b) is to prevent the consumer or the guarantor being required to repay immediately the total amount of the credit without previously having been invited to make good any delay or to submit a proposal for reaching an amicable agreement on the rescheduling of the debt. The Member States must encourage the parties concerned to seek out-of-court agreements or settlements. Two exceptions to this principle are envisaged: manifest fraud and the particular case of the disposal of the property financed, which must be likened to fraud if the consumer has been properly informed in good time concerning the rights to property and privilege enjoyed by the creditor. The fact that the consumer has moved away without leaving an address, even gone abroad, is in itself not enough reason for withholding the default notice. Examples would be hospitalisation or admission to an institution for a long stay, clerical errors by the local authorities, problems with postal deliveries etc.

Paragraph 1(c) covers the suspending of the consumer's rights by the creditor in respect of future credit drawdown. Similar measures may prove indispensable for the creditor in order to rule out fraud or even the manifest indebtedness of the consumer, who might have concealed other credit or who might be facing a court appearance for bankruptcy. In any event the creditor must alert the consumer of his decision, setting out the reasons that prompted him to take the measure in question so that the consumer can, if necessary, contest it before the appropriate courts.

Paragraph 1(d) regulates the provision of statements of account

Article 25 (overrunning of the total amount of credit and tacit overdraft)

The overrunning to which this directive refers implies that a credit agreement already exists. Overrunning or an overdraft where there is no initial agreement runs counter to the general principles of caution and information referred to in this directive. In contrast to the requirements of Article 6 of Directive 87/102/EEC, the charges and rates applicable must be shown in the credit agreement.

The first paragraph deals with the question of authorised overrunning. Tacit overrunning is considered to be the same thing. The conditions are identical to those shown in the credit agreement in relation to the borrowing rate and attendant charges except as regards the total amount of credit that is temporarily overrun.

Paragraph 2 covers unauthorised overrunning. In line with the requirements of Article 10, the additional charges must be shown in the agreement in the form of a statement of cost factors that are not included in the calculation of the annual percentage rate of charge but that are payable by the consumer under certain circumstances.

In both these cases the consumer must be alerted when the account is overrun and advised of the conditions that apply. The situation must be rectified within three months either on the basis of a new credit agreement indicating a higher total amount of credit, by returning to the 'normal' situation or by otherwise terminating the contract or temporarily suspending drawdown.

Article 26 (repossession of goods)

Article 7 of Directive 87/102/EEC makes the recovery of goods a matter for an optional, but not compulsory, court decision. The involvement of a court is necessary to check whether it is appropriate to repossess goods that have been financed when the consumer has shown willingness to repay. A similar check was proposed in the report on the operation of Directive 87/102/EEC ⁽¹⁾. Even if the situation may differ depending on the legal interpretation used ('hire-purchase', loan with subrogation in the rights of the vendor who has expressed a reservation of title, leasing etc.) and the resultant civil and judicial procedures, it is nevertheless proposed that Article 7 should be extended to include provisions guaranteeing the involvement of a third party ⁽²⁾ for all credit agreements when the market value of the goods and the financial interest of the creditor have clearly become less important than the interests of the consumer and the latter has not consented to the repossession of the goods financed.

Article 27 (recovery)

This article refers to any person responsible for enforcing a credit agreement, in other words creditors, credit insurers, recovery agencies etc. but excepts any persons who are responsible for the recovery of money as part of a judicial procedure or for initiating repossession procedures, namely bailiffs. The intention is not to regulate the profession of the 'collection agencies' or 'debt counsellors' but to prohibit certain practices in connection with the non-performance of credit agreements.

⁽¹⁾ Report on the operation of Directive 87/102/EEC for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit — COM(95) 117 final of 11 May 1995 paragraphs 184-188. Summary report of reactions and comments COM(97) 465 final of 24 September 1997, No II.5.

⁽²⁾ Similar or comparable legislation in the MS — non-exhaustive list: B, IRL, NL, L, UK.

The first paragraph confirms a principle that is already established by Article 10: the charges relating to non-performance must be specified in the credit agreement or surety agreement and the persons responsible for collection may not demand more than that which was fixed in the agreement.

Paragraph 2 lists illegal practices.

- the use of envelopes showing words or logos etc. that give the impression that the letter concerned is from an official body, i.e. a judicial authority or a debt counsellor;
- letters threatening the consumer or the guarantor with repossession or prosecution in circumstances where such action is not an option;
- recoveries that disregard the procedures for recovery of goods such as referred to in Article 26 or that entail extra charges that were not detailed in the credit agreement;
- any action that can be likened to a violation of a consumer's or guarantor's privacy, for example harassment in cases where the debt is contested or no longer exists, as well as indirect harassment by contacting a consumer's or guarantor's neighbours, relatives or employers etc. This type of 'doorstep' activity, to which point (f) refers, must involve questions relating to personal data, such as the consumer's 'solvency', that are similar in type to the data to which Article 7 of this directive applies. In principle, information in the public domain relating to changes of address is not considered here.

Article 28 (registration of creditors and credit intermediaries)

This article replaces and extends Article 12 of Directive 87/102/EEC. The proposal is to make it compulsory to take all the steps referred to in Article 12(1) ⁽¹⁾. The introduction of more stringent checks on creditors and credit intermediaries implies that these persons are registered from the outset, that checks are carried out in the first place, that the registration can be suspended or withdrawn (where necessary) and that any complaints are made known. Creditors and credit intermediaries are required, pursuant to this article, to be registered by an official institute or body that will supervise them, in particular monitoring their compliance with the provisions of this directive that are applicable to them.

There is another serious problem in connection with the information that is to be provided for consumers by the 'vendors'. These people frequently do not have the basic knowledge that is required to sell the financial products that they distribute while supervision and statutory requirements in the Member States relating to the quality of the information to be provided by these people and on their suitability to distribute credit are frequently lacking. The solution proposed is to consider them as credit intermediaries and at the same time to make creditors aware of their responsibilities when they resort to vendors as distribution channels for their credit agreements, in particular as regards the provision of information in advance and the duty to offer advice as referred to in Article 6 of this directive and with which credit intermediaries are required to comply. The same status is envisaged for freelance 'delegated agents'. It is still possible for a vendor to work without being under the direct supervision of a creditor, but in this case he must be licensed.

Exceptions are envisaged — as in Directive 87/102/EEC — in relation to creditors and credit intermediaries who are to be considered as credit establishments within the meaning of Article 1(1) of Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions.

Article 29 (obligations of credit intermediaries)

This article contains provisions for special measures in relation to credit intermediaries.

The provision in point (a) establishes the definition of a credit intermediary. Accurate information for consumers must be ensured in relation to the quality and extent of the credit intermediary's powers and on any possible exclusive business connection he has with the creditor so that the consumer does not confuse the intermediary with the creditor.

⁽¹⁾ Similar or comparable legislation in the MS — non-exhaustive list: IRL, UK, and B have merged the three options. NL has provision for a licensing and monitoring system in respect of creditors and this includes a description of their distribution channels plus a separate law on financial intermediaries.

The provision in point (b) is aimed at preventing situations where the intermediary encourages the consumer to contract credit beyond his ability to repay or to opt for a grouping of debts that would be prejudicial to the consumer, in particular by submitting simultaneously two or three credit applications to secure a total amount of credit from several creditors, where each application relates to a small amount which, in itself, may well be acceptable to the creditors individually. However, no creditor would accept funding the total amount of credit being sought. The proposal in point (b) is therefore that intermediaries are to be obliged to inform all creditors that they have previously contacted in connection with an offer or a credit agreement about the total amount of credit being sought.

The provisions in point (c) relate to the regulation of an intermediary's remuneration. It should be remembered that a credit intermediary's commission must be included in the APR. A credit intermediary should not be authorised to contact consumers directly in order to request payment in connection with a credit application or the provision of information unless three conditions are all met:

- the creditor must be informed by a reference to the amount of the fee shown in the credit agreement;
- the credit intermediary shall not be entitled to receive commission from the consumer if he is paid by the creditor;
- the credit agreement must be concluded.

Article 30 (maximum harmonisation and imperative nature of the directive's provisions)

Paragraph 1 confirms the principle of total harmonisation. Member States shall not be entitled to have in place other provisions in relation to the areas covered by this directive unless otherwise stipulated. A similar exception is possible in relation to Article 33 in respect of the burden of proof and in relation to Article 8(4) in connection with the setting-up of a database for positive data. National-level provisions covering maximum or exorbitant APRs or any other type of setting or evaluation of maximum or exorbitant rates may continue to apply. This directive does regulate this area.

Paragraph 2 replaces Article 14(1) of Directive 87/102/EEC and includes the concept of 'guarantor'.

Paragraph 3 retains Article 14(2) and adds another example. The original example spread the total amount of credit over a number of contracts, the lower limit of which allowed an exemption whereas in this current proposal for a directive any reference to lower limits in relation to the scope of the directive has been removed. On the other hand, it must be ensured that the exemptions referred to in Article 3, namely for housing credit and lease agreements, cannot be circumvented so that the transactions covered by this directive can be included in such contracts. In other words, if a consumer requests a credit drawdown under the terms of his housing credit or if, under the terms of his lease contract, he has a tacit option to purchase and the drawdown in question is to allow him to finance the purchase of a car, the directive will apply. Member States are requested to ensure that no such distortion occurs.

Paragraphs 4 and 5 make it clear that the provisions of the directive are imperative. Paragraph 4 lays down that the rights granted to consumers and provided by the directive may under no circumstances be surrendered by consumers.

Paragraph 5 is intended to ensure that consumers' enjoyment of the rights conferred by this directive cannot be denied to them on the grounds that the legislation applicable to the credit agreement or the surety agreement is that of a third country. However, for this rule to apply, it is important that the agreement should have a close link with the jurisdiction of one or more Member States. Similar, identically worded provisions are contained in Directives 93/13/EC relating to unfair terms and 97/7/EC on distance contracts as well as in the Directive of the European Parliament and of the Council of [...] on the distance marketing of consumer financial services modifying Council Directives 90/619/EEC, 97/7/EC and 98/27/EC.

Article 31 (penalties)

The new Article 31 of this proposal for a directive provides that the Member States may impose appropriate penalties on the creditors, etc. concerned who fail to comply with the provisions of national legislation implemented pursuant to this directive. Possibilities include a loss of interest and/or penalties as well as the withdrawal of their licence.

Article 32 (out-of-court redress)

This article is aimed at easing the out-of-court settlement of cross-border disputes by inviting Member States to encourage the bodies responsible for the out-of-court settlement of disputes to cooperate. A cooperation arrangement that could be envisaged is for consumers to contact the out-of-court settlement body in their country of residence which, in turn, would contact its counterpart in the supplier's country. In this way the consumer would not have to pursue the dispute in another Member State. Article 32 is worded in a similar way to the provisions of other directives, such as Article 14 of the Directive of the European Parliament and of the Council of [...] on the distance marketing of consumer financial services modifying Council Directives 90/619/EEC, 97/7/EC and 98/27/EC and which encourages out-of-court settlement in the interests of all concerned.

Article 33 (burden of proof)

Article 33, which is new, is worded in a similar way to the provisions of other directives, such as Article 15 of the Directive of the European Parliament and of the Council of [...] on the distance marketing of consumer financial services modifying Council Directives 90/916/EEC, 97/7/EC and 98/27/EC. The points that have been inserted are necessary to clarify, *inter alia*, the concept of 'credit intermediary'. It has been presumed that the latter works for payment and Member States are free to decide that the burden of proof does not lie with the consumer.

Articles 34 (existing agreements)

This article establishes a transitional arrangement aimed at ensuring that this directive does not apply to existing agreements, specifically long-term credit agreements and open-end credit agreements. Although compulsory references cannot be imposed *ex post* on a credit agreement, on the rules governing responsibility or in relation to the pre-contractual information requirement, it nevertheless remains that a major part of the provisions can and must be applied to existing credit agreements, in particular as regards the information to be given to consumers and guarantors during the performance or in the event of the non-performance of a credit agreement or surety agreement.

Article 36 (repeal)

Article 36 contains formal provisions repealing Directive 87/102/EEC as amended by Directives 90/88/EEC and 98/7/EEC since this directive replaces it.

Articles 35, 37 and 38 (transposition — entry into force — addressees)

These articles contain standard provisions and formulae and require no special comment.

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 95 thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the Economic and Social Committee,

Acting in accordance with the procedure laid down in Article 251 of the Treaty,

Whereas:

- (1) In 1995 the Commission presented a report ⁽¹⁾ on the operation of Council Directive 87/102/EEC of 22 December 1986 on the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit ⁽²⁾, following which it undertook a very broad consultation of the interested parties. In 1997 it presented a summary report of reactions to the 1995 report ⁽³⁾. A second report was produced in 1996 ⁽⁴⁾ on the operation of Council Directive 90/88/EEC of 22 February 1990 amending Directive 87/102/EEC on the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit ⁽⁵⁾.
- (2) These reports and consultations reveal substantial differences between the laws of the various Member States in the field of credit for natural persons in general and consumer credit in particular. Analysis of the national texts transposing Directive 87/102/EEC shows that Member States have considered the degree of protection offered by the directive to be inadequate. They have therefore taken account, in their implementing legislation, of other types of credit and new types of credit agreement not covered by the directive. Consequently, it is necessary to anticipate the reforms of national legislation envisaged by several Member States and to make provision for a harmonised Community framework.
- (3) The *de facto* and *de jure* situation resulting from these national differences leads to distortions of competition among creditors in the Community and restricts consumers' scope for obtaining credit in other Member States. These distortions and restrictions in turn affect the

scale and nature of the demand for cross-border credit, which may have consequences in terms of the demand for goods and services. A further effect of the differences between national laws and practices is that consumers do not enjoy the same protection in all Member States.

- (4) In recent years the types of credit offered to and used by consumers have evolved considerably. New credit instruments have appeared, and their use continues to develop. It is therefore necessary to adapt, amend and complete the existing provisions and to extend their scope.
- (5) It is also necessary to promote the creation of a more transparent and efficient credit market. It is important that this market should offer a degree of consumer protection such that the free movement of credit offers can take place under optimum conditions for both those who offer credit and those who require it. This necessitates a process of maximum harmonisation, to assure all consumers in the Community of a high degree of protection of their interests and an equivalent level of information.
- (6) In view of the growing diversity among the types of credit and credit providers, any person who provides a creditor with information allowing a consumer to be identified and who assists in the conclusion of a credit agreement for a remuneration must be regarded as a credit intermediary, regardless of the form of such remuneration. However, lawyers and notaries should not, in principle, be regarded as credit intermediaries where the consumer contacts them for advice on the scope of a credit agreement or if they help to draft or authenticate an agreement, as long as their role is limited to providing legal or financial advice and they do not direct their clients towards specific creditors.
- (7) Credit agreements covering the granting of credit for the purchase or transformation of immovable property should be excluded from the scope of this directive. This type of credit is of a very specific nature and is the subject of a Commission Recommendation of 1 March 2001 on pre-contractual information to be given to consumers by lenders offering home loans ⁽⁶⁾.
- (8) In view of the risks to their financial interests, the situation of natural persons who stand as guarantors necessitates specific provisions ensuring a level of information and protection comparable to that provided for consumers.

⁽¹⁾ COM(95) 117 final.

⁽²⁾ OJ L 42, 12.2.1987, p. 48. Directive most recently amended by Directive 98/7/EC (OJ L 101, 1.4.1998, p. 17).

⁽³⁾ COM(97) 465 final.

⁽⁴⁾ COM(96) 79 final.

⁽⁵⁾ OJ L 61, 10.3.1990, p. 14.

⁽⁶⁾ OJ L 69, 10.3.2001, p. 25.

- (9) Council Directive 84/450/EEC of 10 September 1984 concerning misleading advertising and comparative advertising ⁽¹⁾ is intended to provide protection with regard to the mention of a figure, cost or rate in advertising or advertising offers relating to a credit agreement. It requires such figure, cost or rate to be accompanied by calculation details making it possible to assess the figure in the context of all the consumer's obligations under a credit agreement.
- (10) In order to ensure real consumer protection, it is necessary to adopt an approach to unsolicited doorstep selling of credit which is stricter than that laid down in Council Directive 85/577/EEC of 20 December 1985 to protect the consumer in respect of contracts negotiated away from business premises ⁽²⁾.
- (11) The provisions of this directive must apply without prejudice to Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data ⁽³⁾. However, a suitable framework for the collection and processing of personal data needed in order to assess the credit risk should be envisaged in certain cases.
- (12) In order to help reduce the credit risk for both the creditor and the consumer, experience and practice testify to the benefits of sufficient and reliable information on cases of default. Member States must therefore ensure that there is a public or private central database in their territory, where appropriate in the form of a network of databases. Consumers and guarantors in the Member State who have defaulted should be registered in this database or network. With a view to working effectively, creditors must be obliged to consult this central database before accepting any commitment on the part of the consumer or guarantor. To prevent any distortion of competition among creditors, it must be ensured that persons and businesses have access to the central database of another Member State under the same conditions as persons and businesses in that Member State, either directly or through the central database of their own Member State.
- (13) In order to ensure the confidentiality of information and protection of personal data, it is essential that the data obtained may be used solely to assess the risk of non-performance by the consumer or guarantor. Any other processing or use of personal data obtained through the central database must be prohibited. Finally, to avoid any risk, the data must be destroyed immediately after the conclusion of the credit agreement or the refusal of the application for credit.
- (14) So that consumers can make their decisions in full knowledge of the facts, they must receive adequate information, prior to the conclusion of the credit agreement, on the conditions and cost of the credit and on their obligations. To ensure absolute transparency and comparability of offers, such information should in particular include the annual percentage rate of charge applicable to the credit, illustrated by a representative example, and the total lending rate.
- (15) In view of the technical and legal complexity of credit instruments, it is necessary to impose a general obligation on the credit intermediary and creditor to provide advice, so that the consumer can choose in full knowledge of the facts among the types of credit offered. Similarly, it is the responsibility of the creditor, in accordance with the principle of 'responsible lending', to check whether the consumer and, where applicable, the guarantor are in a position to meet new commitments.
- (16) The conditions laid down in a credit agreement may in some cases be to the consumer's disadvantage. Better consumer protection must be ensured by imposing certain conditions which apply to all forms of credit. The credit agreement must confirm and add to the information provided before the conclusion of the agreement, where appropriate with the help of an amortisation table and details of the charges for defaulting.
- (17) In view of the specific nature of the terms used in credit and surety agreements, clarification is needed as to which terms are regarded as unfair, without prejudice to the application to the agreement as a whole of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts ⁽⁴⁾.
- (18) In order to approximate the procedures for exercising the right of withdrawal in similar areas, it is necessary to make provision for a right of withdrawal without penalty and with no obligation to provide justification, under conditions similar to those provided for by the Directive of the European Parliament and of the Council of [...] on the distance marketing of consumer financial services and amending Council Directives 90/619/EEC, 97/7/EC and 98/27/EC.

⁽¹⁾ OJ L 250, 19.9.1984, p. 17. Directive amended by Directive 97/55/EC of the European Parliament and of the Council (OJ L 290, 23.10.1997, p. 18).

⁽²⁾ OJ L 372, 31.12.1985, p. 31.

⁽³⁾ OJ L 281, 23.11.1995, p. 31.

⁽⁴⁾ OJ L 95, 21.4.1993, p. 29.

- (19) In order to promote the establishing and functioning of the internal market and ensure a high degree of protection for consumers throughout the Community, it is necessary to fine-tune the method of calculating the annual percentage rate of charge and to determine the components in the total cost of the credit to be used in the calculation. The annual percentage rate of charge is in fact an instrument of comparison allowing the consumer to gauge and compare the impact on his budget, in time and space, of commitments resulting from the conclusion of a credit agreement. The total cost of the credit must therefore include all costs which the consumer is required to pay for the credit, regardless of whether those costs are payable to the creditor, the credit intermediary or any other party. Accordingly, even if the consumer voluntarily takes out insurance on concluding the credit agreement, the costs associated with such insurance must be included in the total cost of the credit.
- (20) It is also necessary to provide the consumer with information, in the form of a total lending rate, on the sums payable to the creditor, excluding those payable to third parties. This rate allows the consumer to compare the costs specific to a creditor in respect of the various products he offers and the various products available on the market.
- (21) The consumer should have the right to discharge his obligations before the due date. In the case of early repayment either in part or in full, the creditor must be entitled to claim a fair and objective indemnity only, and provided that such repayment results in a corresponding financial loss for the creditor.
- (22) If the supplier of goods or services acquired under a credit agreement can be regarded as a credit intermediary, the consumer must be able to enforce rights against the creditor which go further than his normal contractual rights against a supplier of goods or services.
- (23) The transfer of the creditor's rights under a credit agreement must not have the effect of placing the consumer or guarantor in a less favourable position. For the same reasons a creditor who offers a credit agreement providing constitution of capital must assume the risk if the third party providing such constitution of capital defaults on his obligations.
- (24) It is necessary to establish common provisions on measures which apply in the event of non-performance of credit agreements. In particular, certain debt collection practices which are manifestly out of proportion must be considered illegal.
- (25) In order to endure market transparency and stability, Member States need to adopt appropriate measures for the registration of persons offering credit or acting as credit intermediaries with a view to the conclusion of credit agreements, for the inspection or monitoring of creditors and intermediaries, and for enabling consumers to lodge complaints concerning credit agreements or conditions.
- (26) In order to ensure permanent protection of the interests of the consumer and guarantor, credit or surety agreements should not derogate, to the detriment of the consumer or guarantor, from the provisions implementing or corresponding to this directive.
- (27) This directive respects fundamental rights and the principles recognised by the Charter of Fundamental Rights of the European Union. In particular, it aims to ensure full compliance with the rules on protection of personal data, the right to property, non-discrimination, protection of family and professional life, and consumer protection pursuant to Articles 8, 17, 21, 33 and 38 of the Charter.
- (28) Since the objective of this directive, namely to establish rules allowing the harmonisation of the laws, regulations and administrative provisions of the Member States concerning consumer credit, cannot be adequately achieved by the Member States, and can therefore be achieved more effectively at Community level, the Community can take action in accordance with the principle of subsidiarity referred to in Article 5 of the Treaty. In accordance with the principle of proportionality, as referred to in the said Article, this directive does not go beyond what is necessary to achieve these objectives.
- (29) Member States must lay down penalties for infringements of the provisions of this directive and must ensure that they are enforced. These penalties must be effective, proportionate and constitute a deterrent.
- (30) It is therefore necessary to repeal and replace Directive 87/102/EEC,

HAVE ADOPTED THIS DIRECTIVE:

CHAPTER 1

AIM, DEFINITIONS AND SCOPE

Article 1

Aim

The aim of this directive is to harmonise the laws, regulations and administrative procedures of the Member States concerning agreements covering credit granted to consumers and surety agreements entered into by consumers.

Article 2

Definitions

For the purpose of this directive:

- (a) 'consumer' means a natural person who, in transactions covered by this directive, is acting for purposes which can be regarded as outside his trade or profession;
- (b) 'creditor' means a natural or legal person who grants or promises to grant credit in the course of his trade, business or profession;
- (c) 'credit agreement' means an agreement whereby a creditor grants or promises to grant to a consumer credit in the form of a deferred payment, loan or other similar financial accommodation. Agreements for the provision on a continuing basis of services (private or public), where the consumer has the right to pay for them for the duration of their provision by means of instalments, are not deemed to be credit agreements for the purposes of this directive;
- (d) 'credit intermediary' means a natural or legal person who, for a fee, habitually acts as an intermediary by presenting or offering credit agreements, undertaking other preparatory work for such agreements, or concluding such agreements; the fee may take the form of cash or any other agreed form of financial consideration;
- (e) 'surety agreement' means an ancillary agreement concluded by a guarantor and guaranteeing or promising to guarantee the fulfilment of any form of credit granted to natural or legal persons;
- (f) 'guarantor' means a consumer concluding a surety agreement;
- (g) 'total cost of credit to the consumer' means all the costs, including borrowing interest, indemnities, commissions, taxes and any other kind of charge which the consumer has to pay for the credit;
- (h) 'annual percentage rate of charge' means the total cost of the credit to the consumer expressed as an annual percentage of the total amount of credit granted;
- (i) 'sums levied by the creditor' means all the mandatory costs associated with the credit agreement and paid to the creditor by the consumer;
- (j) 'total lending rate' means the sums levied by the creditor expressed as an annual percentage of the total amount of credit;
- (k) 'borrowing rate' means the interest rate expressed as a periodic percentage applied for a given period to the amount of credit drawn down;
- (l) 'residual value' means the purchase price of the financed goods applicable at the time when the purchase option or the property transfer option is exercised;
- (m) 'drawdown' means an amount of credit made available to the consumer in the form of a deferred payment, loan or other similar financial accommodation;
- (n) 'total amount of credit' means the ceiling or the sum of all drawdowns that are likely to be agreed;
- (o) 'durable medium' means any instrument which enables the consumer to store information addressed personally to him in a way which makes it accessible for future reference for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored;
- (p) 'third party providing constitution of capital' means any natural or legal person, other than the creditor or consumer, who gives the consumer or, where applicable, the creditor an undertaking, through an agreement appended to the credit agreement, to constitute the capital to be repaid under such credit agreement.

Article 3

Scope

1. This directive applies to credit agreements and surety agreements.
2. This directive shall not apply to the following credit agreements and, where applicable, any corresponding surety agreements:
 - (a) credit agreements the aim of which is to grant credit for the purchase or transformation of private immovable property that the consumer owns or is seeking to acquire and which are secured either by a mortgage on immovable property or by a surety commonly used in a Member State for this purpose;
 - (b) hiring agreements which exclude the passing of the title to the hirer or to persons entitled by him;
 - (c) credit agreements under the terms of which the consumer is required to repay the credit in a single payment within a period not exceeding three months, without the payment of interest or any other charges;
 - (d) credit agreements which meet the following conditions:
 - (i) they are granted by the creditor as a secondary activity, i.e. outside the sphere of his principal commercial or professional activity,

- (ii) they are granted at annual percentage rates of charge lower than those prevailing on the market,
 - (iii) they are not offered to the public generally;
- (e) credit agreements concluded with investment firms within the meaning of Article 1(2) of Council Directive 93/22/EEC⁽¹⁾ for the purposes of allowing an investor to carry out a transaction relating to one or more of the instruments listed in Section B of the Annex to that directive, where the firm granting the credit is involved in such transaction.

CHAPTER II

INFORMATION AND PRACTICES PRELIMINARY TO THE FORMATION OF THE AGREEMENT*Article 4***Advertising**

Without prejudice to Council Directive 84/450/EEC, any advertising or any offer displayed at business premises that includes information on credit agreements, in particular as regards the borrowing rate, total lending rate and annual percentage rate of charge, shall be provided in a clear and comprehensible manner, with due regard, in particular, to the principles of good faith in commercial transactions. The commercial purpose of this information must be made clear.

*Article 5***Ban on negotiation of credit and surety agreements outside business premises**

The negotiation of a credit or a surety agreement outside business premises in the circumstances referred to in Article 1 of Council Directive 85/577/EEC shall be prohibited.

*Article 6***Exchange of information in advance and duty to provide advice**

1. Without prejudice to the application of Directive 95/46/EC, and in particular Article 6 thereof, the creditor and, where applicable, the credit intermediary may request of a consumer seeking a credit agreement, and any guarantor, only such information as is adequate, relevant and not excessive, with a view to assessing their financial situation and their ability to repay.

The consumer and guarantor shall reply accurately and in full to any such request for information.

2. The creditor and, where applicable, the credit intermediary shall provide the consumer with all the exact and

complete information needed in respect of the credit agreement under consideration. The consumer shall receive this information on paper or on another durable medium before the conclusion of the credit agreement.

Without prejudice to Article 5 of Directive . . . [on the distance marketing of financial services to consumers and amending Council Directives 90/619/EEC, 97/7/EC and 98/27/EC], the information provided must include a concise and clear description of the product, its advantages, and any drawbacks. In particular the information must refer to:

- (a) the sureties and insurance required;
- (b) the duration of the credit agreement;
- (c) the amount, number and frequency of payments to be made;
- (d) the recurrent and non-recurrent charges, including additional non-recurring costs which the consumer has to pay on concluding a credit agreement, such as taxes, administrative costs, legal fees and assessment costs with regard to the sureties required;
- (e) the total amount of credit and the conditions governing the drawdown of the credit;
- (f) where applicable, the cash price of the financed goods or services, the down payment due and the residual value;
- (g) where applicable, the borrowing rate, the conditions governing the application of this rate and any index or reference rate applicable to the initial borrowing rate, as well as the periods, conditions and procedures for varying the borrowing rate;
- (h) the annual percentage rate of charge and the total lending rate, by means of a representative example mentioning all the financial data and assumptions used for calculating the said rates;
- (i) the period during which the right of withdrawal may be exercised.

In the cases referred to in Article 3(3) of Directive . . . [on the distance marketing of financial services to consumers and amending Council Directives 90/619/EEC, 97/7/EC and 98/27/EC], this information must include at least the items referred to in points (c), (e), and (h) of this paragraph.

3. The creditor or, where applicable, the credit intermediary shall seek to establish, among the credit agreements they usually offer or arrange, the most appropriate type and total amount of credit taking into account the financial situation of the consumer, the advantages and disadvantages associated with the product proposed, and the purpose of the credit.

⁽¹⁾ OJ L 141, 11.6.1993, p. 27.

4. Paragraphs 1, 2 and 3 do not apply to suppliers of goods or services acting as credit intermediaries in an ancillary capacity.

CHAPTER III

PROTECTION OF PRIVACY

Article 7

Collection and processing of data

Personal data obtained from consumers, guarantors or any other person in connection with the conclusion and management of agreements covered by this directive, and in particular by Article 6(1), may be processed only for the purpose of assessing the financial situation of those persons and their ability to repay.

Article 8

Central database

1. Without prejudice to the application of Directive 95/46/EC, Member States shall ensure the operation on their territory of a central database for the purpose of registration of consumers and guarantors who have defaulted. This database may take the form of a network of databases.

Creditors must consult the database prior to any commitment on the part of the consumer or guarantor, subject to the restrictions referred to in Article 9.

The consumer and, where appropriate, the guarantor shall, if they so request, be informed of the result of any consultation immediately and without charge.

2. Access to the central database in another Member State shall be ensured under the same conditions as for firms and individuals in that Member State, either directly or via the central database of the home Member State.

3. Personal data received under paragraph 1 may be processed only for the purpose of assessing the financial situation of the consumer and guarantor and their ability to repay. The data shall be destroyed immediately after the conclusion of the credit or surety agreement or the refusal by the creditor of the application for credit or the proposed surety.

4. The central database referred to in paragraph 1 may include the registration of credit agreements and surety agreements.

CHAPTER IV

FORMATION OF CREDIT AND SURETY AGREEMENTS

Article 9

Responsible lending

Where the creditor concludes a credit agreement or surety agreement or increases the total amount of credit or the amount guaranteed, he is assumed to have previously assessed, by any means at his disposal, whether the consumer and, where appropriate, the guarantor can reasonably be expected to discharge their obligations under the agreement.

Article 10

Information that must be included in credit and surety agreements

1. Credit agreements and surety agreements shall be drawn up on paper or on another durable medium.

All the contracting parties, including the guarantor and the credit intermediary, shall receive a copy of the credit agreement. The guarantor shall receive a copy of the surety agreement.

Agreements shall mention the existence or non-existence of out-of-court complaint and redress procedures accessible to consumers who are party to a contract and, if such procedures exist, the formalities for gaining access to them.

2. The credit agreement shall include:

- (a) the names and addresses of the contracting parties as well as the name and address of the credit intermediary involved;
- (b) the data referred to in Article 6(2), with the annual percentage rate of charge and the lending rate calculated at the time the credit agreement is concluded on the basis of all the financial data and assumptions applicable to the agreement;
- (c) where capital amortisation is involved, a statement of account in the form of an amortisation table, the payments owing, and the periods and conditions relating to the payment of these amounts;
- (d) if charges and interest are to be paid without capital amortisation, a statement showing the periods and conditions for the payment of the borrowing interest and of the associated recurrent and non-recurrent charges;
- (e) a statement of the cost components that are not included in the calculation of the annual percentage rate of charge but are to be paid by the consumer under certain circumstances, namely the commitment fee, the charges relating to unauthorised drawdowns in excess of the total amount of credit and the charges for defaulting, plus a list setting out the circumstances;

- (f) where applicable, the goods and/or services being financed;
- (g) entitlement to early repayment, as well as the procedure to be applied by the consumer in order to exercise this right;
- (h) the procedure to be followed to exercise the right of withdrawal.

The table referred to in (c) shall contain a breakdown of each repayment to show capital amortisation, the interest calculated on the basis of the borrowing rate and, where applicable, the additional costs.

If, in the case referred to in (c), a new drawdown is not possible without the consent of the creditor, the creditor's decision shall be communicated on paper or on another durable medium. It shall be made available to the consumer and contain the amended data to which this paragraph refers.

Where the exact amount of these components referred to in (e) is known, it shall be shown. Otherwise, and as a minimum requirement, these costs must be ascertainable in the credit agreement on the basis of an indication of the percentage linked to a reference rate, a calculation method or the most realistic estimate possible. In such cases the creditor shall make available to the consumer on paper or on another durable medium a breakdown of these costs without delay or, at the latest, when they are to be applied.

3. The surety agreement shall state the maximum amount guaranteed, as well as the charges for defaulting to be applied in accordance with the procedure referred to in paragraph 2(e).

Article 11

Right of withdrawal

1. The consumer shall have a period of fourteen calendar days to withdraw his acceptance of the credit agreement without giving any reason.

This period shall begin on the day a copy of the credit agreement concluded is transmitted to the consumer.

2. The consumer shall notify the creditor of his withdrawal before expiry of the period referred to in paragraph 1 and in accordance with national legislation regarding proof. The deadline shall be deemed to have been observed if this notification, which must be on paper or on another durable medium that is available and accessible to the creditor, is dispatched before the deadline expires.

3. Exercise of the right of withdrawal shall oblige the consumer simultaneously to return to the creditor the sums of money or goods that he has received by virtue of the credit agreement, in so far as provision thereof is governed by the credit agreement. The consumer shall pay interest due

for the period during which credit was drawn, calculated on the basis of the agreed annual percentage rate of charge. No other indemnity may be claimed in connection with withdrawal. Any down-payment effected by the consumer under the credit agreement shall be repaid to the consumer without delay.

4. Paragraphs 1, 2 and 3 shall not apply to credit agreements secured by a mortgage or similar surety, credit agreements for housing or credit agreements cancelled under:

- (a) Article 6 of Directive ... [on the distance marketing of financial services to consumers and amending Council Directives 90/619/EC, 97/7/EC and 98/27/EC];
- (b) Article 6(4) of Directive 97/7/EC of the European Parliament and of the Council ⁽¹⁾;
- (c) Article 7 of Directive 94/47/EC of the European Parliament and of the Council ⁽²⁾.

CHAPTER V

ANNUAL PERCENTAGE RATE OF CHARGE AND BORROWING RATE

Article 12

Annual percentage rate of charge

1. The annual percentage rate of charge, which equates, on an annual basis, the present value of all commitments (drawdowns, repayments and charges), future or existing, agreed by the creditor and the borrower, shall be calculated in accordance with the mathematical formula set out in Annex I.

Examples of the method of calculation are given in Annex II, by way of illustration.

2. For the purpose of calculating the annual percentage rate of charge, the total cost of the credit to the consumer shall be determined, with the exception of charges payable by the consumer for non-compliance with any of his commitments laid down in the credit agreement and charges other than the purchase price which, for purchases of goods or services, he is obliged to pay whether the transaction is paid in cash or on credit.

The costs of maintaining an account recording both payment transactions and credit transactions, the costs of using a card or another means of payment for both payment transactions and drawdowns, and the costs relating to payment transactions in general shall be regarded as credit costs unless they have been clearly and separately shown in the credit agreement or in any other agreement concluded with the consumer.

⁽¹⁾ OJ L 144, 4.6.1997, p. 19.

⁽²⁾ OJ L 280, 29.10.1994, p. 83.

Costs relating to insurance premiums shall be included in the total cost of the credit if the insurance is taken out when the credit agreement is concluded.

3. The calculation of the annual percentage rate of charge shall be based on the assumption that the credit contract will remain valid for the period agreed and the creditor and the consumer will fulfil their obligations under the terms and by the dates agreed

4. In the case of credit agreements containing clauses allowing variations in the borrowing rate contained in the annual percentage rate of charge but unquantifiable at the time of calculation, the annual percentage rate of charge shall be calculated on the assumption that the borrowing rate and other charges will remain fixed in relation to the initial level and will remain applicable until the end of the credit agreement.

5. Where necessary, the following assumptions may be adopted in calculating the annual percentage rate of charge:

- (a) if a credit agreement gives the consumer freedom of drawdown, the total amount of credit shall be deemed to be drawn down immediately and in full;
- (b) if there is no fixed timetable for repayment, and one cannot be deduced from the terms of the agreement and the means for repaying the credit granted, the duration of the credit shall be deemed to be one year;
- (c) unless otherwise specified, where the agreement provides for more than one repayment date, the credit will be made available and the repayments made on the earliest date provided for in the agreement;

6. Where a credit agreement is drawn up in the form of a hire agreement with an option to purchase and the agreement provides for a number of dates on which the purchase option may be exercised, the annual percentage rate of charge shall be calculated for each of these dates.

Where the residual value cannot be determined, the goods hired shall be subject to linear amortisation that makes its value equal to zero at the end of the normal hire period laid down in the credit agreement.

7. Where a credit agreement provides for a prior or simultaneous constitution of savings and the borrowing rate is set in relation to these savings, the annual percentage rate of charge shall be calculated in accordance with the procedure set out in Annex III.

Article 13

Total lending rate

1. For the purpose of calculating the total lending rate, the sums levied by the creditor shall be determined, with the

exception of charges payable by the consumer for non-compliance with any of his commitments laid down in the credit agreement and charges other than the purchase price which, for purchases of goods or services, he is obliged to pay whether the transaction is paid in cash or on credit.

2. The costs of maintaining an account recording both payment transactions and credit transactions, the costs of using a card or another means of payment for both payment transactions and drawdowns, and the costs relating to payment transactions in general shall be regarded as sums levied by the creditor unless they have been clearly and separately shown in the credit agreement or in any other agreement concluded with the consumer.

3. The following shall be excluded from the sums levied by the creditor for the purposes of calculating the total lending rate:

- (a) costs associated with ancillary services relating to the credit agreement, which the consumer is free to obtain from the creditor or any other provider;
- (b) costs payable by the consumer on conclusion of the credit agreement to persons other than the creditor, in particular the notary, tax authorities, registrar of mortgages, and any costs in general imposed by the authority responsible for registration and sureties.

4. The total lending rate shall be calculated in accordance with the procedures and assumptions referred to in Article 12(3)-(7) and Annexes I and II.

Article 14

Borrowing rate

1. The borrowing rate may be fixed or variable.

2. Where one or a number of fixed borrowing rates have been established, they shall apply for the duration of the period specified in the credit agreement.

3. A variable borrowing rate may not vary until the end of agreed periods provided for in the credit agreement and may do so only in line with the agreed index or reference rate.

4. The consumer shall be informed of any change to the borrowing rate, on paper or on another durable medium.

This information must include the new annual percentage rate of charge, the creditor's new total lending rate and, where applicable, the new amortisation table. The calculation of the new annual percentage rate of charge and the creditor's new total lending rate shall be based on Article 12(3).

CHAPTER VI

UNFAIR TERMS*Article 15***Unfair terms**

Without prejudice to the application of Directive 93/13/EEC to the agreement as a whole, terms in a credit agreement or surety agreement shall be regarded as unfair if their object or effect is to:

- (a) impose on the consumer, as a condition for a drawdown, a requirement to leave as surety, in full or in part, the sums borrowed or granted, or to use them, in full or in part, to constitute a deposit or purchase securities or other financial instruments, unless the consumer obtains the same rate for such deposit, purchase or surety as the agreed annual percentage rate of charge;
- (b) oblige the consumer, when concluding a credit agreement, to enter into another contract with the creditor, credit intermediary or a third party designated by them, unless the costs thereof are included in the total cost of the credit;
- (c) vary any contractual costs, indemnities or charges other than the borrowing rate;
- (d) introduce rules on the variability of the borrowing rate that discriminate against the consumer;
- (e) introduce a system involving a variable borrowing rate which does not relate to the net initial borrowing rate proposed when the credit agreement was concluded and which would exclude all forms of rebate, reduction or other advantages;
- (f) oblige the consumer to use the same creditor to refinance the residual value and, in general, any final payment on a credit agreement for financing the purchase of movable property or a service.

CHAPTER VII

PERFORMANCE OF A CREDIT AGREEMENT*Article 16***Early repayment**

1. The consumer shall be entitled to discharge fully or partially his obligations under a credit agreement before the time fixed in the agreement.
2. Any indemnity claimed by the creditor for early repayment shall be fair and objective and shall be calculated on the basis of actuarial principles.

No indemnity shall be claimed:

- (a) for credit agreements where the period used to fix the borrowing rate is less than one year;
- (b) if repayment has been made under an insurance contract intended to provide a conventional credit repayment guarantee;
- (c) for credit agreements which provide for payment of charges and interest without capital amortisation, with the exception of the credit agreements referred to in Article 20.

*Article 17***Assignment of rights**

Where the creditor's rights under a credit agreement or surety agreement are assigned to a third party, the consumer and, where applicable, the guarantor, shall be entitled to plead against the assignee of the creditor's rights under that agreement any defence which was available to him against the original creditor, including set-off where the latter is permitted in the Member State concerned.

*Article 18***Ban on the use of bills of exchange and other securities**

The creditor or assignee of the creditor's rights under a credit agreement or surety agreement shall not require or invite the consumer or guarantor to guarantee payment of their commitments under that agreement by means of a bill of exchange or promissory note.

Moreover, the consumer or guarantor shall not be required to sign a cheque guaranteeing repayment, in full or in part, of the amount due.

*Article 19***Joint and several liability**

1. Member States shall ensure that the existence of a credit agreement shall not in any way affect the rights of the consumer against the supplier of goods or services purchased by means of such an agreement in cases where the goods or services are not supplied or are otherwise not in conformity with the contract for their supply.
2. If the supplier of goods or services has acted as credit intermediary, the creditor and the supplier shall be jointly and severally liable for indemnifying the consumer where the goods or services the purchase of which has been financed by the credit agreement are not supplied, or are supplied only in part, or are not in conformity with the contract for their supply.

CHAPTER VIII

SPECIFIC CREDIT AGREEMENTS

Article 20

Credit agreement providing constitution of capital

1. If payments made by the consumer do not give rise to an immediate corresponding amortisation of the total amount of credit, but are used to constitute capital during periods and under conditions laid down in the credit agreement, such constitution of capital shall be based on an ancillary agreement attached to the credit agreement.

2. The ancillary agreement referred to in paragraph 1 shall provide for an unconditional guarantee of repayment of the total amount of credit drawn down. If the third party providing constitution of capital fails to comply with his obligations, the creditor shall assume the risk.

3. Payments, premiums and recurrent or non-recurrent charges payable by the consumer under the ancillary agreement referred to in paragraph 1, together with interest and charges under the credit agreement, shall constitute the total cost of the credit. The annual percentage rate of charge and the total lending rate shall be calculated on the basis of the total commitment subscribed to by the consumer.

Article 21

Credit agreement in the form of an advance on a current account or a debit account

Where a credit agreement covers credit in the form of an advance on a current account or debit account, the consumer shall be regularly informed of his debit situation by means of a statement of account, on paper or on another durable medium, containing the following information:

- (a) the precise period to which the statement of account relates;
- (b) the amounts and dates of drawdowns;
- (c) where applicable, the outstanding balance due from the previous statement, and the date thereof;
- (d) the date and amount of charges due;
- (e) the dates and amounts of payments made by the consumer;
- (f) the last agreed borrowing rate;
- (g) the total amount of interest due;
- (h) where applicable, the minimum amount to be paid;
- (i) where applicable, the new balance outstanding;
- (j) the new total amount outstanding, including any interest on arrears or penalties.

Article 22

Open-end credit agreement

Either party may terminate an open-end credit agreement by giving three months' notice drawn up on paper or on another durable medium in accordance with the procedures laid down in the credit agreement and in accordance with national legislation regarding proof.

CHAPTER IX

PERFORMANCE OF A SURETY AGREEMENT

Article 23

Performance of a surety agreement

1. A guarantor may conclude a surety agreement guaranteeing repayment under an open-end credit agreement for a period of three years only. This surety may be extended only with the specific agreement of the guarantor at the end of that period.

2. The creditor may take action against the guarantor only if the consumer, having defaulted on repayment of the credit, has failed to comply with a default notice within three months.

3. The amount guaranteed may only equal the outstanding balance of the total amount of credit and any arrears in accordance with the credit agreement, with the exclusion of any other indemnities or penalties provided for by the credit agreement.

CHAPTER X

NON-PERFORMANCE OF A CREDIT AGREEMENT

Article 24

Default notice and enforceability

1. Member States shall ensure that:
 - (a) creditors, their representatives and any other assignee of the creditor's rights under a credit agreement or surety agreement may not take disproportionate measures to recover amounts due to them in the event of non-performance of such agreements;
 - (b) the creditor may demand immediate payment in the event of default or invoke a clause providing an express resolute condition only through a prior default notice requesting the consumer or, where applicable, the guarantor to comply with his obligations under the agreement within a reasonable period of time or to apply for rescheduling of the debt;

- (c) the creditor may not suspend the consumer's drawdown rights unless he justifies his decision and is required to inform the consumer without delay;
- (d) in the event of non-performance of their obligations or in the event of early repayment, the consumer and the guarantor are entitled, on request and without delay, to receive a detailed statement of account, free of charge, allowing them to verify the charges and interest claimed.

2. A default notice as referred to in paragraph 1(b) is not necessary:

- (a) in the event of manifest fraud, evidence of which shall be provided by the creditor or the assignee of the creditor's rights;
- (b) where the consumer alienates the property financed before the total amount of credit is repaid or uses the property in a manner inconsistent with the conditions of the credit agreement, and where the creditor or the assignee of the creditor's rights has a preferential claim, right of possession or reservation of title on the property financed, provided that the consumer has been informed of the existence of such preferential claim, right of possession or reservation of title prior to the conclusion of the contract.

Article 25

Overrunning of the total amount of credit and tacit overdraft

1. In the event of an authorised temporary overrunning of the total amount of credit or a tacit overdraft, the creditor shall inform the consumer without delay, in writing or on another durable medium, of the amount involved and the borrowing rate applicable. No penalties, charges or interest on arrears shall be included.

2. The creditor shall inform the consumer without delay that he has overrun the credit amount or is in an unauthorised overdraft situation and shall inform him of the borrowing rate and/or the charges or penalties applicable.

3. Any overrunning or overdraft as referred to in this article shall be rectified within three months, where necessary through a new credit agreement providing for a higher total amount of credit.

Article 26

Repossession of goods

In the case of credit agreements for the acquisition of goods, Member States shall lay down the conditions under which goods may be repossessed. If the consumer has not given his

specific consent at the moment the creditor proceeds for repossession and if he has already made payments corresponding to a third of the total amount of credit, the goods financed may not be repossessed unless by judicial proceedings.

Member States shall further ensure that, where the creditor repossess the goods, the account between the parties is made up so as to ensure that repossession does not entail any unjustified enrichment.

Article 27

Recovery

1. Natural or legal persons who undertake, as their principal or as a secondary activity, and not as part of any court procedure, the recovery of debts arising from a credit agreement or surety agreement, or who intervene in this respect, may not, in any form whatsoever, either directly or indirectly, claim any fee or indemnity from the consumer or guarantor for their intervention, unless such fees or indemnities are specifically agreed in the credit agreement or surety agreement.

2. In the context of the recovery of debts arising from a credit agreement or surety agreement, the following shall be prohibited:

- (a) any document which, as a result of its appearance, wrongly gives the impression that it is from a judicial or debt mediation authority;
- (b) written communications containing incorrect information on the consequences of defaulting on payment;
- (c) unauthorised repossession of goods without judicial proceedings or the specific consent referred to in Article 26;
- (d) any inscription on an envelope which makes it clear that the correspondence concerns the recovery of a debt;
- (e) collection of charges not provided for by the credit agreement or surety agreement;
- (f) any contact with the neighbours, relatives or employer of the consumer or guarantor, especially any communication of, or request for, information on the solvency of the consumer or guarantor, without prejudice to actions forming part of statutory seizure procedures as established by Member States;
- (g) physical or psychological harassment of a consumer or guarantor;
- (h) recovery of a lapsed debt.

CHAPTER XI

**REGISTRATION, STATUS AND CONTROL OF CREDITORS
AND CREDIT INTERMEDIARIES***Article 28***Registration of creditors and credit intermediaries**

1. Member States shall ensure that creditors and credit intermediaries apply for registration.

The obligation to register does not apply to credit intermediaries for whom a creditor or another credit intermediary assumes responsibility under the terms of his own registration. This assumption of responsibility must be made clear in a notice on the premises of credit intermediaries not required to register.

2. Member States shall:

(a) ensure that the activities of creditors and credit intermediaries are subject to inspection or monitoring by an institution or official body;

(b) establish appropriate bodies to receive complaints concerning credit agreements, surety agreements and credit and surety conditions, and to provide consumers and guarantors with relevant information or advice on this subject.

3. Member States may stipulate that registration as referred to in the first subparagraph of paragraph 1 of this article shall not be necessary where the creditor or credit intermediary concerned is a 'credit institution' within the meaning of Article 1(1) of Directive 2000/12/EC of the European Parliament and of the Council⁽¹⁾ and is authorised in accordance with the provisions of that directive.

Where a creditor or credit intermediary is both registered under the provisions of the first subparagraph of paragraph 1 of this article and authorised under the provisions of Directive 2000/12/EC of the European Parliament and of the Council, and the latter authorisation is subsequently withdrawn, the competent authority which has registered the creditor or credit intermediary shall be informed and shall decide whether the creditor or credit intermediary may continue to grant or arrange credit or whether his registration should be cancelled.

*Article 29***Obligations of credit intermediaries**

Member States shall ensure that a credit intermediary:

(a) indicates in advertising and documentation intended for clients the extent of his powers, in particular whether he works exclusively with one or more creditors or as an independent broker;

(b) communicates to all creditors contacted the total amount of other credit offers he has requested or received for the same consumer or guarantor during the two months preceding conclusion of the credit agreement;

(c) does not receive, directly or indirectly, any fee, in whatever form, from a consumer who has requested his services, unless all the following conditions are met:

(i) the amount of the fee is stated in the credit agreement,

(ii) the credit intermediary does not receive a fee from the creditor,

(iii) the credit agreement for which he has acted is actually concluded.

CHAPTER XII

FINAL PROVISIONS*Article 30***Total harmonisation and imperative nature of the directive's provisions**

1. Member States may not introduce provisions other than those laid down in this directive, except with regard to:

(a) registration of credit agreements and surety agreements in accordance with Article 8(4);

(b) the provisions concerning the burden of proof referred to in Article 33.

2. Member States shall ensure that credit agreements and surety agreements do not derogate, to the detriment of the consumer or guarantor, from the provisions of national law implementing or corresponding to this directive.

3. Member States shall further ensure that the provisions they adopt in implementation of this directive cannot be circumvented as a result of the way in which agreements are formulated, in particular by integrating drawdowns or credit agreements falling under the scope of this directive into credit agreements the character or purpose of which would make it possible to avoid its application.

4. Consumers and guarantors may not waive the rights conferred on them by this directive.

5. Member States shall take the measures needed to ensure that the consumer and the guarantor do not lose the protection granted by this directive by virtue of the choice of the law of a non-member country as the law applicable to the agreement, if the agreement has a close link with the territory of one or more Member States.

⁽¹⁾ OJ L 126, 26.5.2000, p. 1.

Article 31

Penalties

Member States shall lay down penalties for infringements of national provisions adopted in application of this directive, and shall take all necessary measures to ensure that these are enforced. These penalties must be effective, proportionate and constitute a deterrent. They may provide for the loss of interest and charges by the creditor and continuation of the right of repayment in instalments of the total amount of credit by the consumer, in particular where the creditor does not respect the provisions on responsible lending. Member States shall communicate these provisions to the Commission no later than [...] [2 years after the entry into force of this directive] and any subsequent amendments concerning them without delay.

Article 32

Out-of-court redress

Member States shall ensure that adequate and effective complaints and redress procedures for the out-of-court settlement of consumer disputes concerning credit and surety agreements are put in place, using existing bodies where appropriate.

Member States shall encourage bodies responsible for the out-of-court settlement of consumer disputes to cooperate in order to resolve cross-border disputes concerning credit and surety agreements.

Article 33

Burden of proof

Member States may provide that the burden of proof in respect of compliance with the consumer information obligations imposed on the creditor and credit intermediary, in respect of the consumer's consent to the conclusion of the contract and, where appropriate, its performance, and in respect of the credit intermediary's remunerated activities may lie with the creditor or credit intermediary.

Any term in an agreement which provides that the burden of proof in respect of compliance by the creditor and, where applicable, the credit intermediary with all or part of the obligations incumbent on them pursuant to this directive should lie with the consumer and, where applicable, the guarantor, shall be an unfair term within the meaning of Directive 93/13/EEC.

Article 34

Existing agreements

1. This directive does not apply to credit agreements and surety agreements existing on the date the national implementing measures enter into force, with the exception of the provisions of Articles 1, 2, 3 and 22, 23(1) and (2), 24 to 27, and 30 to 35. Article 9 shall apply to such contracts

in so far as an increase in the total amount of credit or the amount guaranteed occurs after the national measures implementing this directive enter into force.

2. For agreements existing on the date the national implementing measures enter into force, the amortisation table referred to in Article 10 must be provided to the consumer free of charge as soon as either of the following conditions applies:

- (a) cancellation of the credit agreement or early repayment;
- (b) default on payment.

3. Member States shall ensure that open-end credit agreements and surety agreements existing on the date the national implementing measures enter into force have to be replaced by new agreements which comply with this directive no later than [...] [two years after the end of the transposition period].

Article 35

Transposition

Member States shall adopt and publish, no later than [...] [2 years after the entry into force of this directive] the laws, regulations and administrative provisions necessary to comply with this directive. They shall immediately inform the Commission thereof.

They shall apply these provisions from [...] [2 years after the entry into force of this directive].

When Member States adopt these provisions, these shall contain a reference to this directive or shall be accompanied by such reference at the time of their official publication. Member States shall determine how such reference is to be made.

Article 36

Repeal

Directive 87/102/EEC is repealed with effect from [...] [the end of the transposition period for this directive].

Article 37

Entry into force

This directive shall enter into force on the twentieth day following its publication in the *Official Journal of the European Communities*.

Article 38

Addressees

This directive is addressed to the Member States.

ANNEX I

THE BASIC EQUATION EXPRESSING THE EQUIVALENCE OF DRAWDOWNS ON THE ONE HAND AND REPAYMENTS AND CHARGES ON THE OTHER

The basic equation, which establishes the annual percentage rate of charge (APR), equates, on an annual basis, the total present value of drawdowns on the one hand and the total present value of repayments and payments of charges on the other hand, i.e.:

$$\sum_{k=1}^m C_k (1 + X)^{-t_k} = \sum_{l=1}^{m'} D_l (1 + X)^{-s_l}$$

where:

- X is the APR
- m is the number of the last drawdown,
- k is the number of a drawdown, therefore $1 \leq k \leq m$,
- C_k is the amount of drawdown k ,
- t_k is the interval, expressed in years and fractions of a year, between the date of the first drawdown and the date of each subsequent drawdown, therefore $t_1 = 0$,
- m' is the number of the last repayment or payment of charges,
- l is the number of a repayment or payment of charges,
- D_l is the amount of a repayment or payment of charges,
- s_l is the interval, expressed in years and fractions of a year, between the date of the first drawdown and the date of each repayment or payment of charges.

Remarks:

- (a) The amounts paid by both parties at different times shall not necessarily be equal and shall not necessarily be paid at equal intervals.
- (b) The starting date shall be that of the first drawdown.
- (c) Intervals between dates used in the calculations shall be expressed in years or in fractions of a year. A year is presumed to have 365 days (or 366 days for leap years), 52 weeks or 12 equal months. An equal month is presumed to have 30,41666 days (i.e. $365/12$) regardless of whether or not it is a leap year.
- (d) The result of the calculation shall be expressed with an accuracy of at least one decimal place. If the figure at the following decimal place is greater than or equal to 5, the figure at that particular decimal place shall be increased by one.
- (e) The equation can be rewritten using a single sum and the concept of flows (A_k), which will be positive or negative, in other words either paid or received during periods 1 to k , expressed in years, i.e.:

$$S = \sum_{k=1}^n A_k (1 + X)^{-t_k}$$

S being the present balance of flows. If the aim is to maintain the equivalence of flows, the value will be zero.

- (f) Member States shall provide that the methods of resolution applicable give a result equal to that of the examples presented in Annexes II and III.

ANNEX II

EXAMPLES OF CALCULATION OF THE ANNUAL PERCENTAGE RATE OF CHARGE

Preliminary remarks

Unless otherwise stated, all examples assume a single drawdown of credit equal to the total amount of the credit and placed at the consumer's disposal as soon as the credit agreement is concluded. In this connection, it should be noted that if the credit agreement gives the consumer freedom of drawdown, the total amount of credit is deemed to be drawn down immediately and in full.

Some Member States, in order to express the borrowing rate, have opted for an effective rate and the equivalent conversion method, thus avoiding a situation in which the calculation of periodical interest is carried out in countless ways using different *pro rata temporis* rules which have only a very vague relationship with the linear nature of time. Other Member States permit a nominal periodic rate using a proportional conversion method. This directive seeks to separate any further regulation of borrowing rates from the regulation of effective rates, simply stating the rate used. The examples in this Annex refer to the method that has been used.

Example 1

Total amount of credit (capital) of EUR 6 000,00, repayable in four equal annual instalments of EUR 1 852,00.

The equation becomes:

$$6\,000 = 1\,852 \frac{1 - \frac{1}{(1+X)^4}}{X}$$

or:

$$6\,000 = 1\,852 \frac{1}{(1+X)^1} + 1\,852 \frac{1}{(1+X)^2} + \dots + 1\,852 \frac{1}{(1+X)^4}$$

giving $X = 9,00000\%$, i.e. an APR of 9,0 %.

Example 2

Total amount of credit (capital) EUR 6 000,00, repayable in 48 equal monthly instalments of EUR 149,31.

The equation becomes:

$$6\,000 = 149,31 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{48}}}{(1+X)^{1/12} - 1}$$

or:

$$6\,000 = 149,31 \frac{1}{(1+X)^{1/12}} + 149,31 \frac{1}{(1+X)^{2/12}} + \dots + 149,31 \frac{1}{(1+X)^{48/12}}$$

giving $X = 9,380593\%$, i.e. an APR of 9,4 %.

Example 3

Total amount of credit (capital) of EUR 6 000,00, repayable in 48 equal monthly instalments of EUR 149,31. Administrative charges of EUR 60,00 are payable on conclusion of the contract.

The equation becomes:

$$6\,000 - 60 = 149,31 \frac{1 - \frac{1}{[(1 + X)^{1/12}]^{48}}}{(1 + X)^{1/12} - 1}$$

or:

$$5\,940 = 149,31 \frac{1}{(1 + X)^{1/12}} + 149,31 \frac{1}{(1 + X)^{2/12}} + \dots + 149,31 \frac{1}{(1 + X)^{48/12}}$$

giving $X = 9,954966\%$, i.e. an APR of 10 %.

Example 4

Total amount of credit (capital) of EUR 6 000,00, repayable in 48 equal monthly instalments of EUR 149,31. Administrative charges of EUR 60,00 are spread over the repayments. The monthly instalment is therefore (EUR 149,31 + (EUR 60/48)) = EUR 150,56.

The equation becomes:

$$6\,000 = 150,56 \frac{1 - \frac{1}{[(1 + X)^{1/12}]^{48}}}{(1 + X)^{1/12} - 1}$$

or:

$$6\,000 = 150,56 \frac{1}{(1 + X)^{1/12}} + 150,56 \frac{1}{(1 + X)^{2/12}} + \dots + 150,56 \frac{1}{(1 + X)^{48/12}}$$

giving $X = 9,856689\%$, i.e. an APR of 9,9 %.

Example 5

Total amount of credit (capital) of EUR 6 000,00, repayable in 48 equal monthly instalments of EUR 149,31. Administrative charges are EUR 60,00, and insurance EUR 3,00 per month. The costs associated with insurance premiums must be included in the total cost of the credit if the insurance is taken out when the credit agreement is concluded. The instalment is therefore EUR 152,31.

The equation becomes:

$$5\,940 = 152,31 \frac{1 - \frac{1}{[(1 + X)^{1/12}]^{48}}}{(1 + X)^{1/12} - 1}$$

or:

$$5\,940 = 152,31 \frac{1}{(1 + X)^{1/12}} + 152,31 \frac{1}{(1 + X)^{2/12}} + \dots + 152,31 \frac{1}{(1 + X)^{48/12}}$$

giving $X = 11,1070115\%$, i.e. an APR of 11,1 %.

Example 6

Balloon-type credit agreement for a total amount of credit of EUR 6 000,00 (purchasing price of a car to be financed), repayable in 47 equal monthly instalments of EUR 115,02 plus a final payment of EUR 1 915,02 representing the residual value of 30 % of the capital (balloon agreement), plus insurance of EUR 3,00 per month. Again, the costs associated with insurance premiums must be included in the total cost of the credit if the insurance is taken out when the credit agreement is concluded. The instalment is therefore EUR 118,02, and the final payment will amount to EUR 1 918,02.

The equation becomes:

$$6\,000 = 118,02 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{47}}}{(1+X)^{1/12} - 1} + 1\,918,02 \frac{1}{[(1+X)^{1/12}]^{48}}$$

or:

$$6\,000 = 118,02 \frac{1}{(1+X)^{1/12}} + 118,02 \frac{1}{(1+X)^{2/12}} + \dots + 118,02 \frac{1}{(1+X)^{47/12}} + \\ (1\,800 + 115,02 + 3) \frac{1}{(1+X)^{48/12}}$$

giving $X = 9,381567\%$, i.e. an APR of $9,4\%$.

Example 7

Credit agreement for a total amount of credit (capital) of EUR 6 000,00 with administrative charges of EUR 60,00 payable on conclusion of the contract, and two payment periods of 22 and 26 months respectively. The second-period instalment corresponds to 60 % of the first-period instalment. The respective monthly instalments are EUR 186,36 and EUR 111,82.

The equation becomes:

$$5\,940 = 186,36 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{22}}}{(1+X)^{1/12} - 1} + \left\{ \left[111,82 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{26}}}{(1+X)^{1/12} - 1} \right] \frac{1}{[(1+X)^{1/12}]^{22}} \right\}$$

or:

$$5\,940 = \left[186,36 \frac{1}{(1+X)^{1/12}} + 186,36 \frac{1}{(1+X)^{2/12}} + \dots + 186,36 \frac{1}{(1+X)^{22/12}} \right] + \\ \left\{ \left[111,82 \frac{1}{(1+X)^{1/12}} + 111,82 \frac{1}{(1+X)^{2/12}} + \dots + 111,82 \frac{1}{(1+X)^{26/12}} \right] \frac{1}{[(1+X)^{1/12}]^{22}} \right\}$$

giving $X = 10,04089\%$, i.e. an APR of $10,0\%$.

Example 8

Credit agreement for a total amount of credit (capital) of EUR 6 000,00, with administrative charges of EUR 60,00 payable on conclusion of the contract, and two payment periods of 22 and 26 months respectively, the first-period instalment corresponding to 60 % of the second-period instalment. The respective monthly instalments are EUR 112,15 and EUR 186,91.

The equation becomes:

$$5\,940 = 112,15 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{22}}}{(1+X)^{1/12} - 1} + \left\{ \left[186,91 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{26}}}{(1+X)^{1/12} - 1} \right] \frac{1}{[(1+X)^{1/12}]^{22}} \right\}$$

or:

$$5\,940 = \left[112,15 \frac{1}{(1+X)^{1/12}} + 112,15 \frac{1}{(1+X)^{2/12}} + \dots + 112,15 \frac{1}{(1+X)^{22/12}} \right] + \\ \left\{ \left[186,91 \frac{1}{(1+X)^{1/12}} + 186,91 \frac{1}{(1+X)^{2/12}} + \dots + 186,91 \frac{1}{(1+X)^{26/12}} \right] \frac{1}{[(1+X)^{1/12}]^{22}} \right\}$$

giving $X = 9,888383\%$, i.e. an APR of $9,9\%$.

Example 9

Credit agreement for a total amount of credit (price of goods) of EUR 500,00 repayable in three equal monthly instalments calculated by applying the borrowing rate T of 18 % (nominal rate), plus administrative charges of 30,00 spread over the payments. The monthly instalment is therefore EUR 171,69 + EUR 10,00 charges = EUR 181,69.

The equation becomes:

$$500 = 181,69 \frac{1 - \frac{1}{[(1 + X)^{1/12}]^3}}{(1 + X)^{1/12} - 1}$$

or:

$$500 = 181,69 \frac{1}{(1 + X)^{1/12}} + 181,69 \frac{1}{(1 + X)^{2/12}} + 181,69 \frac{1}{(1 + X)^{3/12}}$$

giving $X = 68,474596$ %, i.e. an APR of 68,5 %.

This example typifies practices still used by certain specialist 'vendor-credit' establishments.

Example 10

Credit agreement for a total amount of credit (capital) of EUR 1 000, repayable in two instalments of either EUR 700,00 after one year and EUR 500,00 after two years, or EUR 500,00 after one year and EUR 700,00 after two years.

The equation becomes:

$$1\ 000 = 700 \frac{1}{[(1 + X)^{1/12}]^{12}} + 500 \frac{1}{[(1 + X)^{1/12}]^{24}}$$

giving $X = 13,898663$ %, i.e. an APR of 13,9 %.

or:

$$1\ 000 = 500 \frac{1}{[(1 + X)^{1/12}]^{12}} + 700 \frac{1}{[(1 + X)^{1/12}]^{24}}$$

giving $X = 12,321446$ %, i.e. an APR of 12,3 %.

This example shows that the annual percentage rate of charge depends on the payment periods and that stating the total cost of the credit in the prior information or in the credit agreement is of no benefit to the consumer. Despite the total cost of credit being EUR 200 in both cases, there are two different APRs (depending on the speed of repayment).

Example 11

Credit agreement for a total amount of credit of EUR 6 000,00, with a borrowing rate of 9 %, repayment in four equal annual instalments of EUR 1 852,01, and administrative charges of EUR 60,00 payable on conclusion of the agreement.

The equation becomes:

$$5\ 940 = 1\ 852,01 \frac{1 - \frac{1}{(1 + X)^4}}{X}$$

or:

$$5\ 940 = 1\ 852,01 \frac{1}{(1 + X)} + 1\ 852,01 \frac{1}{(1 + X)^2} + \dots + 1\ 852,01 \frac{1}{(1 + X)^4}$$

giving $X = 9,459052\%$, i.e. an APR of 9,5 %.

In the event of early repayment, the equations become:

After one year:

$$5\,940 = 6\,540 \frac{1}{(1 + X)}$$

where 6 540 is the sum due, including interest, before payment of the first scheduled payment according to the amortisation table,

giving $X = 10,101010\%$, i.e. an APR of 10,1 %.

After two years:

$$5\,940 = 1\,852,01 \frac{1}{(1 + X)} + 5\,109,91 \frac{1}{(1 + X)^2}$$

where 5 109,91 is the sum due, including interest, before payment of the second scheduled payment according to the amortisation table,

giving $X = 9,640069\%$, i.e. an APR of 9,6 %.

After three years:

$$5\,940 = 1\,852,01 \frac{1}{(1 + X)} + 1\,852,01 \frac{1}{(1 + X)^2} + 3\,551,11 \frac{1}{(1 + X)^3}$$

where 3 551,11 is the sum due, including interest, before payment of the third scheduled payment according to the amortisation table,

giving $X = 9,505315\%$, i.e. an APR of 9,5 %.

This shows how the provisional APR decreases in the course of time, especially where charges are payable on conclusion of the agreement.

This example can also serve to illustrate the case of a mortgage credit intended to refinance current credit agreements where the costs (notary's fees, registration, taxes) are due when the authenticated act is completed and the funds are made available to the consumer from the same date.

Example 12

Credit agreement for a total amount of credit of EUR 6 000, with a borrowing rate T of 9 % (nominal rate), repayment in 48 monthly instalments of EUR 149,31 (calculated proportionally), and administrative charges of EUR 60,00 payable on conclusion of the agreement.

The equation becomes:

$$5\,940 = 149,31 \frac{1 - \frac{1}{[(1 + X)^{1/12}]^{48}}}{(1 + X)^{1/12} - 1}$$

or:

$$5\,940 = 149,31 \frac{1}{(1 + X)^{1/12}} + 149,31 \frac{1}{(1 + X)^{2/12}} + \dots + 149,31 \frac{1}{(1 + X)^{48/12}}$$

giving $X = 9,9954957\%$, i.e. an APR of 10 %.

However, in the case of early repayment, this becomes:

After one year:

$$5\,940 = 149,31 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{11}}}{(1+X)^{1/12} - 1} + 4\,844,64 \frac{1}{[(1+X)^{1/12}]^{12}}$$

where 4 844,64 is the sum due, including interest, before payment of the 12th scheduled payment according to the amortisation table,

giving $X = 10,655907\%$, i.e. an APR of 10,7 %.

After two years:

$$5\,940 = 149,31 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{23}}}{(1+X)^{1/12} - 1} + 3\,417,58 \frac{1}{[(1+X)^{1/12}]^{24}}$$

where 3 417,58 is the sum due, including interest, before payment of the 24th monthly instalment according to the amortisation table,

giving $X = 10,136089\%$, i.e. an APR of 10,1 %.

After three years:

$$5\,940 = 149,31 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{35}}}{(1+X)^{1/12} - 1} + 1\,856,66 \frac{1}{[(1+X)^{1/12}]^{36}}$$

where 1 856,66 is the sum due, including interest, before payment of the 36th monthly instalment according to the amortisation table,

giving $X = 9,991921\%$, i.e. an APR of 10 %.

Example 13

Total amount of credit (capital) of EUR 6 000,00, repayable in four equal annual instalments of EUR 1 852,00. Let us now assume that the borrowing rate (nominal rate) is variable and increases from 9,00 % to 10,00 % after the second annual instalment. This results in a new annual instalment of EUR 1 877,17. Remember that, in calculating the APR, it is normally assumed that the borrowing rate and other costs remain fixed at the initial level and apply until the end of the credit agreement. In that case (example 1), the APR will be 9 %.

In the event of any change to the rate, the new APR must be communicated and calculated on the assumption that the credit agreement will remain in force for the rest of the agreed duration, and that the creditor and consumer will fulfil their obligations under the terms and by the dates agreed.

The equation becomes:

$$5\,940 = 1\,852,01 \frac{1 - \frac{1}{(1+X)^2}}{X} + \left[1\,877,17 \frac{1 - \frac{1}{(1+X)^2}}{X} \frac{1}{X^2} \right]$$

or:

$$5\,940 = 1\,852,01 \frac{1}{(1+X)} + 1\,852,01 \frac{1}{(1+X)^2} + \left\{ \left[1\,877,17 \frac{1}{(1+X)^3} + 1\,877,17 \frac{1}{(1+X)^4} \right] + \frac{1}{X^2} \right\}$$

giving $X = 9,741569\%$, i.e. an APR of 9,7 %.

Example 14

Total amount of credit (capital) of EUR 6 000,00, repayable in 48 equal monthly instalments of EUR 149,31, with administrative charges of EUR 60,00 payable on conclusion of the agreement, plus insurance of EUR 3,00 per month. The costs associated with insurance premiums must be included in the total cost of the credit if the insurance is taken out when the credit agreement is concluded. The instalment is therefore EUR 152,31 and the calculation, as in example 5, gives $X = \text{EUR } 11,107112$, i.e. an APR of 11,1 %.

Let us now assume that the borrowing rate (nominal) is variable and increases to 10 % after the 17th payment. This change requires a new APR to be communicated and calculated on the assumption that the credit agreement will remain in force for the rest of the agreed duration, and that the creditor and consumer will fulfil their obligations under the terms and on the dates agreed.

The equation becomes:

$$5\,940 = 151,91 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{17}}}{(1+X)^{1/12} - 1} + \left[154,22 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{31}}}{(1+X)^{1/12} - 1} \frac{1}{[(1+X)^{1/12}]^{17}} \right]$$

or:

$$5\,940 = \left[151,91 \frac{1}{(1+X)^{1/12}} + 151,91 \frac{1}{(1+X)^{2/12}} + \dots + 151,91 \frac{1}{(1+X)^{17/12}} \right] + \left\{ \left[154,22 \frac{1}{(1+X)^{1/12}} + 154,22 \frac{1}{(1+X)^{2/12}} + \dots + 154,22 \frac{1}{(1+X)^{31/12}} \right] \frac{1}{[(1+X)^{1/12}]^{17}} \right\}$$

giving $X = 11,542740$ %, i.e. an APR of 11,5 %.

Example 15

Credit agreement of the 'leasing' type for a car with a value of EUR 15 000. The agreement stipulates 48 monthly instalments of EUR 350. The first monthly instalment is payable as soon as the car is placed at the consumer's disposal. At the end of the 48 months the purchase option may be taken up by paying the residual value of EUR 1 250.

The equation becomes:

$$14\,650 = 350 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{47}}}{(1+X)^{1/12} - 1} + 1\,250 \frac{1}{[(1+X)^{1/12}]^{48}}$$

or:

$$14\,650 = 350 \frac{1}{(1+X)^{1/12}} + 350 \frac{1}{(1+X)^{2/12}} + \dots + 350 \frac{1}{(1+X)^{47/12}} + 1\,250 \frac{1}{(1+X)^{48/12}}$$

giving $X = 9,541856$ %, i.e. an APR of 9,5 %.

Example 16

Credit agreement of the 'financing', 'vendor credit' or 'hire purchase' type for goods with a value of EUR 2 500. The credit agreement provides for a down-payment of EUR 500 plus 24 monthly instalments of EUR 100, the first of which must be paid within 20 days of the goods being placed at the consumer's disposal.

In such cases the down-payment is never part of the financing operation.

The equation becomes:

$$(2\,500 - 500) \frac{1}{\left[(1 + X)^{1/365}\right]^{[365 \cdot 20]}} = 100 \frac{1 - \frac{1}{\left[(1 + X)^{1/12}\right]^{24}}}{(1 + X)^{1/12} - 1}$$

or:

$$2\,000 \frac{1}{(1 + X)^{\frac{10\,4316}{365}}} = 100 \frac{1}{(1 + X)^{1/12}} + 100 \frac{1}{(1 + X)^{2/12}} + \dots + 100 \frac{1}{(1 + X)^{24/12}}$$

giving $X = 20,395287$, i.e. an APR of 20,4 %.

Example 17

Credit agreement for a credit line of EUR 2 500 for a period of six months. The credit agreement provides for payment of the total cost of the credit every month and repayment of the total amount of the credit at the end of the agreement. The annual borrowing rate (effective rate) is 8 %, and the charges amount to 0,25 % per month. The assumption that the amount of credit is drawn down immediately and in full applies here.

The monthly borrowing interest payment is calculated on the basis of an equivalent monthly rate, using the equation:

$$a = 2\,500 \left\{ \left[(1,08)^{1/12} - 1 \right] + 0,25 \right\}$$

or:

$$a = 2\,500 (0,006434 + 0,0025) = 22,34$$

This becomes:

$$2\,500 = 22,34 \frac{1 - \frac{1}{\left[(1 + X)^{1/12}\right]^6}}{(1 + X)^{1/12} - 1} + 2\,500 \frac{1}{(1 + X)^{6/12}}$$

This becomes:

$$2\,500 = 22,34 \frac{1}{(1 + X)^{1/12}} + 22,34 \frac{1}{(1 + X)^{2/12}} + \dots + 22,34 \frac{1}{(1 + X)^{6/12}} + 2\,500 \frac{1}{(1 + X)^{6/12}}$$

giving $X = 11,263633$, i.e. an APR of 11,3 %.

Example 18

Credit agreement for an open-end credit line of EUR 2 500. The agreement provides for a minimum half-yearly payment of 25 % of the outstanding balance (capital and interest), with a minimum of EUR 25. The annual borrowing rate (effective rate) is 12 %, and the administrative charge payable on conclusion of the agreement is EUR 50.

(The equivalent monthly rate is obtained by the equation:

$$i = (1 + 0,12)^{6/12} - 1 = 0,00583$$

or 5,83 %).

The 19 half-yearly repayments (D_t) can be obtained from an amortisation table, giving $D_1 = 661,44$; $D_2 = 525$; $D_3 = 416,71$; $D_4 = 330,75$; $D_5 = 262,52$; $D_6 = 208,37$; $D_7 = 165,39$; $D_8 = 208,37$; $D_9 = 104,20$; $D_{10} = 82,70$; $D_{11} = 65,64$; $D_{12} = 52,1$; $D_{13} = 41,36$; $D_{14} = 32,82$; $D_{15} = 25$; $D_{16} = 25$; $D_{17} = 25$; $D_{18} = 25$; $D_{19} = 15,28$.

The equation becomes:

$$2\,500 - 50 = 661,44 \frac{1}{(1+X)^{6/12}} + 525 \frac{1}{(1+X)^{12/12}} + \dots + 25 \frac{1}{(1+X)^{108/12}} + 15,28 \frac{1}{(1+X)^{114/12}}$$

giving $X = 13,151744\%$, i.e. an APR of 13,2 %.

Example 19

Credit agreement for an open-end credit line involving the use of a card for drawdowns. Total amount of the credit: EUR 700. The agreement provides for a minimum monthly payment of 5 % of the outstanding balance (capital and interest), and the scheduled instalment (a) may not be less than EUR 25. The annual cost of the card is EUR 20. The annual borrowing rate (effective rate) is 0 % for the first instalment and 12 % for the subsequent instalments.

The 31 monthly repayment amounts (D_t) can be obtained from an amortisation table, giving $D_1 = 55,00$; $D_2 = 33,57$; $D_3 = 32,19$; $D_4 = 30,87$; $D_5 = 29,61$; $D_6 = 28,39$; $D_7 = 27,23$; $D_8 = 26,11$; $D_9 = 25,04$; D_{10} à $D_{12} = 25,00$; $D_{13} = 45$; D_{14} à $D_{24} = 25,00$; $D_{25} = 45$; D_{26} à $D_{30} = 25,00$; $D_{31} = 2,25$.

The equation becomes:

$$700 = 55 \frac{1}{(1+X)^{1/12}} + 33,57 \frac{1}{(1+X)^{2/12}} + \dots + 25 \frac{1}{(1+X)^{30/12}} + 2,25 \frac{1}{(1+X)^{31/12}}$$

giving $X = 18,470574$, i.e. an APR of 18,5 %.

Example 20

Open-end credit line in the form of an advance on a current account. Total amount of credit: EUR 2 500. The credit agreement does not impose any requirements in terms of repayment of capital, but provides for monthly payment of the total cost of the credit. The annual borrowing rate is 8 % (effective rate). The monthly charges amount to EUR 2,50.

It is assumed that the full amount of credit will be drawn down, with repayment in theory after one year.

First of all, the theoretical scheduled payment of interest and charges (a) is calculated

$$a = 2\,500 \left[(1,08)^{1/12} - 1 \right] + 2,50$$

then:

$$2\,500 = 18,59 \frac{1 - \frac{1}{\left[(1+X)^{1/12} \right]^{12}}}{(1+X)^{1/12} - 1} + 2\,500 \frac{1}{(1+X^{1/12})^{12}}$$

i.e.:

$$2\,500 = 18,59 \frac{1}{(1+X)^{1/12}} + 18,59 \frac{1}{(1+X)^{2/12}} + \dots + 18,59 \frac{1}{(1+X)^{12/12}} + 2\,500 \frac{1}{(1+X)^{12/12}}$$

giving $X = 9,295804$, i.e. an APR of 9,3 %.

ANNEX III

**CALCULATION OF THE ANNUAL PERCENTAGE RATE OF CHARGE FOR A CONTRACT REQUIRING
ADVANCE OR ACCOMPANYING SAVINGS AND FOR WHICH THE BORROWING RATE IS SET TO
REFLECT THE LEVEL OF SAVINGS**

Symbols used:

- C = Capital
- N = duration in years
- T = annual borrowing rate
- A = annuity
- F = periodicity
- n = duration in periods
- t = periodic borrowing rate
- a = periodic repayment
- M = saving period

1. MIXED CREDIT AGREEMENT WITH (COMPULSORY) SAVINGS IN ADVANCE

First example

The granting of a credit C totalling EUR 6 000 over N = two years is subject to the saving in advance over M = two years of half of the said amount, i.e. EUR 3 000 in all, of which the final amount saved is EUR 125 and is deposited one month prior to the drawdown of the credit. The savings in question attract no interest but the borrowing rate for the credit agreement will amount to no more than T = 6 % at a time when market conditions are setting a rate of 9 % instead.

The amount saved each month is e = EUR 125,00, the monthly repayment a = EUR 140,91, the APR, excluding savings, is 6,17 % or 6,2 %.

To find the annual percentage rate applicable to the transaction as a whole the formula is as follows:

$$6\,000 + 3\,000 = \left[125 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{24}}}{(1+X)^{1/12} - 1} [(1+X)^{1/12}]^{25} \right] + \left[140,91 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{48}}}{(1+X)^{1/12} - 1} \right]$$

or:

$$6\,000 + 3\,000 = \left\{ \left[125 \frac{1}{(1+X)^{1/12}} + 125 \frac{1}{(1+X)^{2/12}} + \dots + 125 \frac{1}{(1+X)^{24/12}} \right] [(1+X)^{1/12}]^{25} \right\} + \left[140,91 \frac{1}{(1+X)^{1/12}} + 140,91 \frac{1}{(1+X)^{2/12}} + \dots + 140,91 \frac{1}{(1+X)^{48/12}} \right]$$

To solve the equation using a recursive method, let $X_1 = 0,062$, and the value of the first member calculated as 170,5.

then $X_2 = 0,063$ and the value of the first member is calculated as 163,3.

and so forth

then $X_{26} = 0,087$ and the value of the first member is calculated at 6,0.

then $X_{27} = 0,088$ and the value of the first member is calculated at 0,1.

then $X_{28} =$ and the value of the first member is calculated at -5,7.

The correct solution is $X = 8,802245\%$, or 8.8% and this is the APR to be given to the consumer as the APR for the credit agreement involving an amount to be saved in advance.

Second example

The granting of a credit C totalling EUR 6 000 over $N =$ two years is subject to the saving in advance over $M =$ two years of half of the said amount, i.e. EUR 3 000 in all, of which the final amount saved is EUR 125 and is deposited one month prior to the drawdown of the credit. These savings attract a lending rate of $S = 3\%$ and the borrowing rate is only $T = 6\%$ at a time when market conditions set rates at 9% .

The amount saved each month is $e =$ EUR 125,00, the monthly repayment $a =$ EUR 140,91, the APR, excluding savings is $6,17\%$ or 6.2% .

The updated future value of M will be M' calculated according to the following formula:

$$M' = 125 \frac{(1+i)^n - 1}{i}$$

where $i = (1+S)^{1/12} - 1$ and $n = 24$ months.

or:

$$M'(t_{-1}) = 125 \frac{(1,03)^{24/12} - 1}{(1,03)^{1/12} - 1} = 3\,086,65$$

and

$$M'(t_0) = 3\,086,65(1,03)^{1/12} = 3\,094,26$$

where $t_0 =$ time of credit drawdown.

To find the APR for the transaction as a whole:

$$3\,094,26 + 6\,000 = \left[125 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{24}}}{(1+X)^{1/12} - 1} [(1+X)^{1/12}]^{25} \right] + \left[140,91 \frac{1 - \frac{1}{[(1+X)^{1/12}]^{48}}}{(1+X)^{1/12} - 1} \right]$$

or:

$$3\,094,26 + 6\,000 = \left\{ \left[125 \frac{1}{(1+X)^{1/12}} + 125 \frac{1}{(1+X)^{2/12}} + \dots + 125 \frac{1}{(1+X)^{24/12}} \right] [(1+X)^{1/12}]^{25} \right\} + \left[140,91 \frac{1}{(1+X)^{1/12}} + 140,91 \frac{1}{(1+X)^{2/12}} + \dots + 140,91 \frac{1}{(1+X)^{48/12}} \right]$$

To solve the equation a recursive method can again be used with $X = 7,484710$, or an APR of $7,5\%$.

2. MIXED AGREEMENT WITH ACCOMPANYING SAVINGS

2.1. **Mixed credit agreement with optional savings (advances to current account)**

See Annex II, example 20. Savings do not form part of the APR calculation.

2.2. **Credit agreement with mixed life assurance**

These are endowment-type mortgages such as those referred to in Article 20 of this directive, where saving forms part of the agreement.

Let the total amount of credit be EUR 6 000 to be repaid in four annuities at a borrowing rate of 9 % but structured as repayments *in fine*. Suppose that the manager of the fund has paid at the end of each of the three first years an amount of 1 200 and that this amount saved has attracted 4 %. The balance of this account, before the final repayment is due, will be EUR 3 895,76. It will then be necessary for him to add an additional EUR 2 104,24. His timetable will be for three annuities at EUR 1 740,00 and one at EUR 2 644,24 for a capital of EUR 6 000.

The formula:

$$6\,000 = 1\,740 \frac{1 - \frac{1}{(1+X)^3}}{X} + 2\,644,24 \frac{1}{(1+X)^4}$$

or:

$$6\,000 = 1\,740 \frac{1}{(1+X)^1} + 1\,740 \frac{1}{(1+X)^2} + 1\,740 \frac{1}{(1+X)^3} + 2\,644,24 \frac{1}{(1+X)^4}$$

and $X = 10,955466$, or an APR of 10,96 %.
