



Position paper by the Finanzplatz München Initiative (FPMI)

Meeting with Commissioner Kuneva in Brussels on June 27, 2007

Core statements

A. EU consumer-protection policy in the financial-services sector

- Consumer-protection policy should be based on the perception of the consumer as a responsible and informed individual.
- EU-wide harmonisation of all consumer-protection provisions should be driven forward.
- No need for consumer class actions

B. Uniform European contract law

- The FPMI welcomes the efforts of the Commission and the European Parliament to establish a basis for uniform European contract law
- The principle of contractual freedom must be respected.
- In the interest of easily understandable classifications, it is desirable to have uniform regulations for basic contract law (e.g. entering into contracts, specifications of obligations, and sanctions in case of breach of contract).

C. Mortgage credits

- Instead of a directive concerning mortgage credits and new binding rules concerning pre-contractual information, the existing voluntary Code of Conduct should be reviewed and amended so that it can be implemented by the banking industry throughout the EU.
- The German banking industry and the German government unanimously refuse the establishment of a legal right to early repayment for consumers even if there would be compensations for the creditor.



D. Consumer Credit Directive

- The greatest possible degree of full harmonisation should be achieved. The many exceptions in the political agreement reached by the Council of the European Union on May 21, 2007, create diverging consumer protection standards and distortions of competition.
- A high level of consumer protection is to be guaranteed. At the same time the market participants are not to be burdened with unnecessary bureaucratic requirements and unnecessary costs. The Council's proposal does not largely meet this requirement. The FMPI advocates the reduction of mandatory information obligations to a level that permits an easy overview.
- The Council's intended revision of the consumer credit directive will make it impossible to continue offering the customary overdraft facility ("Dispositionskredit") in Austria and in Germany in the simple, non-bureaucratic form currently in use, thus making this form of credit significantly more expensive. This could prove seriously detrimental, with this particularly applying to the poorer segments of the population. The proposal of the Council is not in line with its own declared intention of requiring overdraft facilities to comply only with "a few" information obligations.
- Limited early repayment fees will result in higher borrowing costs and destroy the German culture of taking out credits with long-term terms of interest. The FMPI views the urgent need to continue with intensive discussions on early repayments as also stemming from the enormous potential for claims being lodged with German banks.



A. Positions on EU consumer-protection policy in the financial-services sector

1. Perception of the consumer as a responsible and informed individual

The EU's consumer-protection policy should be guided by the perception of the consumer as a responsible and informed individual. Among other things this means that the consumer does not require unnecessary protective regulations, such as those pertaining to advisory services. Consumers have to be put into the position of being able to decide for themselves whether they want any information and advice before buying financial services and, if so, how much. An exaggerated amount of consumer protection inevitably goes hand in hand with higher costs. These are ultimately borne by the customer. Therefore any harmonisation of consumer-protection rules among the individual member states should not lead to an automatic adaptation to the highest common denominator in consumer protection. Rather, the existing regulations set up by national legal systems must be subjected to critical scrutiny, so as to establish whether they perceive the consumer as a responsible and informed individual and are really necessary from the point of view of consumer protection.

2. Harmonisation of consumer-protection rules across the EU

As the Commission explains in its communication on the EU's consumer-policy strategy for the years 2007 to 2013, consumer lack of trust is one impediment to the creation of a single European market. Regulatory impediments are others – especially those regarding financial services as legal product. Thus, a supplier of financial services who wants to offer its products in another EU member state may well find that certain of its contractual conditions do not apply, as they contravene legal provisions of that other member state. The harmonisation of individual consumer-protection rules cannot fully do away with these regulatory obstacles. It is therefore necessary to systematically harmonise all consumer-protection rules in order to remove the impediments to the cross-border distribution of financial products and to thereby promote competition. In addition, no member state should be allowed to adopt more stringent measures than those in force at the EU level. A reciprocal recognition of contractual provisions among the member states should be taken into consideration as an interim move towards full harmonisation.

3. Facilitated choice of law/ Rome I Regulation

One of the biggest obstacles to creating a fully functional EU-wide single market in the financial-services sector is the only very limited possibility to agree on the



law applicable to the supplier. This is particularly true in the field of insurance where the present choice of law is governed by the insurance directives of the second and third generation, which only allow freedom of choice for policies relating to major risks. This is even true if the policyholder is an entrepreneur. The incorporation of the Rome Convention on the Law Applicable to Contractual Obligations into the Rome I Regulation should be used in order to integrate the conflict-of-laws rules applicable to insurance contracts into the general conflict-of-laws system and abolish the currently valid special conflict-of-laws rules for insurance contracts. However, the present proposal on the Rome I Regulation results in a restriction of the choice of law compared with the Rome Convention. Whereas the Rome Convention follows the agreed contract law – with only the imperative regulations of the consumer’s home member state applying if they are more in the consumer’s favour – according to the draft of the Rome I Regulation the law applicable to consumer contracts is always to be that of the state in which the consumer habitually resides. In the opinion of the FPMI this is a step in the wrong direction. In order to create a barrier-free market for financial services, the choice of law has to be made easier, not more difficult.

4. No need for consumer class actions

In its communication on consumer-policy strategy the Commission gave consideration to permitting the lodging of consumer class actions against violations of the consumer-protection rules and against breaches of EU anti-trust legislation. A legal instrument of that nature should be strictly rejected. It would result in a tide of US-style class actions – in the USA a full-blown “class-action industry” has come into being. The trouble is that only a small part of the compensation payments awarded actually go to the claimants, with the lion’s share going to the attorneys, who are skilled at using the class-action procedure to their own benefit. These actions do not make the legal system any more efficient. In fact, class actions place a considerable burden on the US economy. This undesirable development defeats the actions’ original purpose in the USA of effectively protecting consumer interest. It must be avoided in Europe at all costs. The FPMI has issued an urgent warning about the belief that a “European way” of conducting class actions could avoid these negative developments.



B. Uniform European contract law

The FPMI welcomes the efforts of the Commission and the European Parliament to establish a basis for uniform European contract law. This is initially to take the form of a Common Reference Framework. We see it as having the potential to promote trade in goods and services. If the national contract law of individual countries is pushed into the background – with a certain amount of inconvenience for foreign contract partners – particularly mid-sized enterprises could benefit from uniform contract law.

The Commission itself stated in its White Paper on Financial Services Policy for 2005–2010 (Com (2005) 629 final) that every Commission proposal will be accompanied by impact assessments. In the current situation we see no sign of these assessments having been made. However, to preclude years of discussions in various circles and committees, an impact assessment should be carried out. It should focus on the costs and benefits to consumers and companies of a „Common Reference Framework“ as described above.

Despite the above, and even if a uniform European code of contract law is still a long way off, it is already possible from our standpoint to list the following points that have to be addressed in the ongoing discussions and considerations:

1. The principle of contractual freedom must be respected

The principles of contractual freedom must remain the starting point of any uniform European contract law (ROME I) enacted in the years to come. In relations between businesses and consumers, it is not acceptable for the interests of either side to take unilateral precedence. For European legislators it will be a major challenge to master the reconciliation of these interests. This challenge arises in the distinguishing between individual agreements and general terms and conditions of business. The definition of general terms and conditions of business and the extent of court control are therefore of particular importance.

2. Uniform regulation of the basic principles of contract law

In the interest of easily understandable classifications it is desirable to have uniform regulations for basic contract law (e.g. entering into contracts, specifications of obligations, and sanctions in case of breach of contract).



3. Uniform case law

Uniform European contract law will be capable of creating a single unified market and of facilitating and expediting cross-border trade only if it is uniformly applied by national courts. It should therefore be considered whether this responsibility requires the establishment of a new judicial authority within the European Court of Justice, or whether it is sufficient to provide a reliable, generally accessible database (including whenever possible any required translations).

4. Responsibility for developing the “Common Reference Framework”

We suggest transferring responsibility for formulating the Common Reference Framework, which is currently under the exclusive jurisdiction of the Directorate General for Health and Consumer Protection, to the Directorate General for Justice, Freedom, Security and the Internal Market. Another possibility would be to provide for shared jurisdiction. Doing such would ensure that the General Reference Framework and the other projects in the area of civil and contract law such as the Convention on the Law Applicable to Contractual Obligations (ROME I) are mutually compatible.



C. Integration of mortgage credit markets

Concerning the integration of mortgage credit markets, we have by now received the Commission's Green Paper dated 19th July 2005 and the statements rendered at the consultations of expert groups, organisations and others. The White Paper concerning mortgage credits is to be published in June 2007.

In line with the German government we are of the opinion, that the benefits of a further integration of mortgage credit markets have neither been properly investigated nor demonstrated. It is for these reasons that we welcome the commission's plan for an impact study.

We would like to examine in detail the following issues, which we consider important in conjunction with expediting the integration of mortgage credit markets:

1. Information for consumers

Instead of enacting a directive concerning mortgage credits and new binding rules concerning pre-contractual information, the existing voluntary Code of Conduct should be reviewed and amended so that it can be implemented by the banking industry throughout the EU.

We share the general opinion that the provision of pre-contractual information to consumers is very important. This information is to be given by ESIS, which has already been implemented in Germany and only a few other Member States via the Code of Conduct. It has therefore created a precedent for standardising pre-contractual information at the EU level.

2. No right to early repayment

A consumer in Germany already has the choice between mortgage loans with fixed interest and without the right to early repayment, and those bearing floating rates and with the right to early repayment. The popularity of mortgage credits in form of fixed-rate loans is based on their providing substantially better rates of interest, as compared to loans with floating rates. The reason why the former bear more favourable rates of interest terms is that fixed-rate loans are often refinanced, at superior conditions, on the capital market, via the matching maturities provided by mortgage bonds („Pfandbriefe“).

The German banking industry and the German government unanimously refuse



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the creation of a legal right to early repayment for consumers even in those cases in which creditors would be recompensed. If a large amount of borrowers would repay their fixed-rate loans early (especially when interest rates are declining), the value of the mortgages covering the bonds would also rapidly fall. This would impact the quality of the Pfandbrief-cover which would cause a potentially negative effect for the Pfandbrief-holders. This in turn would lead to increasing costs for Pfandbriefe and, thus, to those borne by mortgage credits. A legal right to early repayment would have thus a negative effect on this funding system and especially upon the fixed-rate loans which are so very popular with German consumers.

We oppose a legal right of early repayment without compensation or with a simple flat rate of compensation because these compensation rules would interfere with the control mechanisms in place in the banking industry concerning liquidity and interests. Due to the fact that the banking industry would offset the potential losses by factoring these into the prices levied for mortgage credits, this rule would penalise those consumers who do not use their right of early repayment. In the end, the costs of a legal right of early repayment would be shared by all borrowers.

3. Developing and implementing of a Euromortgage

Developing and implementing of a Euromortgage which is not strictly accessory would be a great step forward in integrating the European mortgage credit markets. It would especially open up more opportunities for borrowers to generate cross-border-credits and for the banking industry new possibilities in cross-border-funding.

4. No admission of non-deposit taking institutions

We oppose (in agreement with the ZKA and the German Government) allowing non-deposit taking institutions to offer mortgage credits. The facts that the banking industry have to meet higher capital requirements and are subject to strict supervision pose competitive disadvantages vis-à-vis such institutions. Another potential problem created by the licensing of such institutions would be their negative effects on the stability of the capital market.

5. Harmonisation of valuation standards

We join the German Government in pushing for a harmonisation of valuation standards. This would have positive impact on the comprehensibility and



comparability of valuations, and would thus facilitate the ongoing integration of mortgage credit markets. It is crucial that this harmonisation be carried out on a high level through the application of comprehensible criteria: The standardisations must not lead to a lowering of the standards currently prevailing in Germany, and particularly those involving the German Pfandbrief Act.

To ensure the recoverability of those Pfandbriefe which are issued to finance mortgage credits, it is imperative to maintain a high standard of valuation, in our opinion. Lowering the valuation standards would in turn lead to higher rates of interest being borne on Pfandbriefe, and, thus, to the charging of higher interest rates on mortgage credits.



D. Consumer Credit Directive

1. The greatest possible degree of full harmonisation will benefit the European Single Market

For the establishment of a uniform market for consumer credit in Europe – which is considered an explicit goal of the Directive – the aim must be to achieve the greatest possible degree of full harmonisation. This is the only way of ensuring the fair cross-border competition which results in favourable terms for the consumer. Every step towards the achieving of a minimal harmonisation diametrically contravenes this objective. The many exceptions contained in the political agreement concluded by the Council of the European Union on May 21, 2007, will produce unequal consumer protection standards and distortions of competition.

Needed to be found are balanced regulations that are acceptable to all concerned parties and which are implemented at the same, uniform level in all member states. The achieving of this essential prerequisite for a uniform market will make it possible for consumers and companies to reap full benefit.

The establishment of a uniform Single Market is dependent upon no barriers being created at the nation level through the enacting of formal regulations.

2. Disempowerment of the consumer and unsatisfactory liability

The European Commission also advocates the concept of the “empowered consumer.” However, this cannot be reconciled with the liability concept in the Draft Directive, which, through the “Principle of Responsible Lending,” assigns very extensive responsibility to the bank, also with regard to the transaction being financed. The principle must continue to apply that the consumer himself makes the final decision on whether or not to take out a loan. The FPMI is vehemently opposed to this form of consumer disempowerment because it assigns to financial institutions the responsibility of protecting consumers “against themselves.”

Banks are today required under banking supervision laws to ascertain the creditworthiness of their customers before granting loans. The conversion of the regulatory requirement to check creditworthiness into a civil-law obligation to the consumer would result in the imposition of a new liability tort on the credit industry. It would enable a consumer who is unable to repay a loan to claim damages due to both an alleged failure to provide proper information on the disadvantages of the credit product, and to an improper check of his creditworthiness. This regulation contradicts the guiding principle of the empowered consumer proclaimed by the Commission.



3. Bureaucratic and excessive information requirements demonstrate a lack of knowledge of banking practice

The standard information provided in advertising materials (Article 4) is superfluous because, according to the Draft Directive, the consumer must be informed in writing anyway before signing the contract. In addition, there already exist enough European-level regulations that provide protection of consumers against false or misleading advertising.

The standard information required in advertising should at least be defined to accord to the media (e.g. radio, television) of its propagation.

It also cannot be in the interest of consumer protection for consumers to be flooded with information, before signing the contract, that they do not need and perhaps cannot even use. A widespread observation is that the – possibly well meant – flood of information results in the intended recipients being unable or unwilling to filter out the important and relevant information. The FPMI therefore advocates the lowering of mandatory information obligations to a level that permits an easy overview. The FMPI is committed, of course, to the principle of meeting requests by consumers for clarifications of credit terms and conditions for consumers; however, we are emphatically opposed to the notion that lenders should have an obligation to automatically provide consumers with a flood of information on a routine basis. Consequently, the Draft Directive should be amended to limit information requirements to what is necessary.

This petition is supported by the results of the study conducted by Civic Consulting Alleweldt & Kara GbR. The study was commissioned by the European Parliament and published on April 25, 2007. The study concludes that the unclear and very complex regulations will result in greater uncertainty on the part of consumers. With this in mind, the authors recommend to start by making a comprehensive investigation of consumer needs, among other things. This is long overdue. We therefore wish to emphasize our support for this proposal.

4. The draft legislation would impose unnecessary obstacles to the granting of overdraft facilities and make them more expensive

The intended revision of the consumer credit directive will make it impossible to continue offering the customary overdraft facility (“Dispositionskredit”) in Austria and in Germany in the simple, non-bureaucratic form currently in use, thus making this form of credit significantly more expensive. This could prove particularly and seriously detrimental to the poorer segments of the population. The proposal of the Council does not accord with its own declared intention of requiring overdraft



facilities to comply only with “a few” information obligations. On the contrary, the quantity of information obligations does not differ substantially from those of other credit contracts. Efforts must be made to ensure that overdraft facilities can still be granted with a minimum of bureaucratic hurdles. The information obligations must be limited to those that are actually needed to facilitate consumers’ being granted an overdraft facility. The FPMI demands that the applicable regulations be lowered to an appropriate level.

5. Limited early repayment fees will result in higher borrowing costs and destroy the German long-term interest culture

According to the proposal the Council agreed upon, it is possible to repay fixed-interest loans at any time, with this also applying to the fixed-interest period, by paying an early repayment fee equal to 1 percent of the amount of the loan, or just 0.5 percent if less than one year remains in the fixed-interest period. There is no reasonable justification for limiting the early repayment fee to 1 percent or 0.5 percent. It also contradicts general principles on compensation for damages, which state that the party causing the damage must compensate the party incurring the damage in full for the entire amount. A regulation like the one proposed would have substantial detrimental effects on the formulation of terms and conditions. This is because banks would have to take into account the potential losses resulting from such a regulation – which, according to initial calculations, may amount to untold millions! – when setting their prices. In the final analysis, therefore, this would result in allocating to society as a whole the losses resulting from the individual loan agreement due to the premature repayment.

The Council’s proposal would also have a considerable negative impact on competitiveness, with this particularly applying to the fixed-interest products that enable consumers to plan with certainty—something not arising from products bearing variable terms. This would be particularly detrimental to the German banking sector, in which, unlike in most other EU states, fixed-interest loans remain commonplace. This would also mean the destruction of the German culture of taking out loans bearing long terms of interest, as the obligation to dispense with early repayment fees would mean the end of the issuing of 5–10-year fixed-interest loans at low interest rates.

The Consumer Credit Directive should be made to preserve product neutrality, however, and should not unilaterally favour products with variable terms. It should be left up to the consumer to choose freely among the available products on the basis of accurate information and fair competition.

The FPMI therefore still pleads for the retention of the exact actuarial calculation



of the early repayment fee for each individual loan in line with the approach that has emerged under German jurisdiction. This is the fairest solution for all parties concerned.

Alternatively, it would also be conceivable to enact a percentage compensation rule applying only to an acceptable residual fixed-interest period, and, for other cases to apply an exact actuarial calculation or at least a calculation method that takes the essential factors into account (the prevailing interest-rate climate when the loan agreement was signed and at the time of repayment as well as the remaining fixed-interest period).

This would be a compromise solution that would probably be readily acceptable to most European countries, as fixed-interest periods significantly longer than one year are apparently relatively rare in other countries, at least in the consumer lending sector. It would also be a decisive help to the banks in Germany.

In addition, early repayment at any time during the fixed-interest period should be possible only for important reasons (e.g. unemployment, divorce, death) because this possibility also has to be included in the pricing of loans, hence making them more expensive.

In any case the FPMI sees an urgent need to continue with intensive discussions on early repayments also in view of the enormous damages potentially facing German banks.

Another helpful step would be for an expert committee, possibly including (neutral) experts from the Bundesbank or the ECB, to further examine this issue.