



## European Banking Industry Committee

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European Banking Federation (EBF) • European Savings Banks Group (ESBG) • European Association of Cooperative Banks (EACB) European Mortgage Federation (EMF) • European Federation of Building Societies (EFBS)  
European Federation of Finance House Associations (Eurofinas)/European Federation of Leasing Company Associations (Leaseurope)  
European Association of Public Banks (EAPB)

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### **EBiC Position on the Integration of the European Financial Markets**

#### **1. General ambitions for the further development of a single financial market**

##### **An integrated and competitive market**

1. EBiC agrees with the findings of the experts in all FSAP expert group reports that there is no need for a new extensive programme of regulatory measures.
2. In EBiC's view the securities and wholesale markets are more integrated while further progress in the retail banking market could still be achieved. It has to be noted however, that the means to achieve integration should not be strictly of a legislative kind, and non-legislative measures should be also considered (e.g. in the payments area).
3. The European banking sector is pluralist (diversity of providers of financial services) in structure and EBiC considers this an important characteristic which should be maintained, if European banking markets are to remain competitive, provided however that there is the same level playing field for all kind of institutions and that there is no distortion of competition.

##### **Consumer and investor confidence: crucial for an integrated market**

4. EBiC is of the view that any European legislative measures aiming to improve the level of integration in financial services should have the expectations, needs and requirements of individual consumers and investors in mind. At the same time, the regulatory environment should enable the financial services industry to meet these consumer expectations without undue bureaucratic constraints. In this context, EBiC welcomes the FIN-Net initiative.
5. EBiC firmly believes that a key issue which is touched on in the banking expert group report but is not subject to any firm recommendations is the need for transparency with regard to product information. It is only by being able to make clear and like for like comparisons that the consumer will be able to compare products from different providers. It is essential that transparency exists at this level if the industry is to gain consumers' trust with regards to the provision of cross-border financial services.
6. A prerequisite for increased economic growth is the promotion of consumer and investor confidence. This will foster the necessary conditions to increase their willingness to engage in Europe's financial markets. This is an important responsibility, not only for regulators and policy-makers, but also of the industry.

**Retail banking: targeted harmonization needed.**

7. One way of promoting an integrated market and equally enhance consumer confidence would potentially be to harmonize consumer protection provisions at the EU level. Different harmonization approaches have been used over time such as minimum harmonization and full/maximum harmonization. Minimum harmonization in theory provides a fairly modest level of harmonization but allows Member States to introduce, or maintain, more stringent requirements by means of their national legislation. Maximum/full harmonization, in contrast, would prevent Member States from introducing more stringent provisions.
8. The minimum harmonization approach has been predominantly used in the past but its application has not helped to promote integration as Member States have complemented the text of the EU directive by (often different) national provisions. Recent experience with maximum/full harmonisation<sup>1</sup> reveals that this harmonisation approach has tended to equate to the highest possible levels of harmonization, given the fact that Member States are prevented from introducing provisions others than those laid down by any given directive. To further illustrate this argument, reference can be made to the FSC report, where Member State representatives are quoted as saying that “full harmonisation may fail to reflect differences in consumer preferences, business models and other factors between Member States”. Experience at Council level shows that Member States tend to insist on integrating their highest consumer protection rules. As a result, the industry and customers alike are faced with unworkable legislation leading ultimately to higher costs, and not operating in the interests of any of the stakeholders<sup>2</sup>.
9. In this context, EBIC is in favour of “targeted harmonization”, i.e. full *harmonization of those key provisions* which would facilitate further integration (as outlined in paragraph 11 below). In the EC banking report on integration, the pursuit of targeted harmonization is supported as one of the means of removing “unjustified or unreasonable obstacles to market entry”. It is the belief of EBIC that promoting such a pragmatic and flexible approach to policymaking will improve the effectiveness of EU legislation.
10. EBIC would however strongly advise against product and services standardisation via legislation as it would likely lead to market distortions. It should be left to financial institutions to design banking products in response to customer needs and to reflect the economic realities of the market. In that context, EBIC has taken note of the commissioning by DG Sanco of a study on product standardization which is currently being drafted by Charles River Associates, and it is very much hoped that EBIC will be fully consulted on the issue in due course.
11. In concrete terms, EBIC recommends that targeted harmonization be undertaken in the following areas (see annex 1 for details):
  - Definition of the consumer
  - Pre-contractual information requirements
  - Annual Percentage Rate of Charge
  - Right of withdrawal
  - Rules for on-line identification and authentication
  - Contracting online;
  - Recognising equivalence of ‘KYC’ standards;

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<sup>1</sup> See 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, COM(2002) 443 final.

<sup>2</sup> See footnote above.

12. Alternative Dispute Resolution (ADR) Systems: EBIC welcomes the Commission's FIN-NET initiative of establishing an informal contact point network to address consumers' disputes related to financial services. FIN-NET provides consumers with a first point of support, which is extremely valuable in a cross-border situation. This way, costly and lengthy judicial procedures can be avoided. The special merit of FIN-NET is that it makes efficient use of existing national schemes, rather than try and harmonize the existing bodies.

Against this background, EBIC is not in favour of introducing harmonized binding rules related to consumers' redress systems such as the European Code of Conduct for all kind of mediators - as suggested by the Commission in its Green Paper<sup>3</sup> and lately by DG JAI. EBIC strongly feels that the merits of industry-developed schemes, based on flexible and informal resolutions, continue to be the most optimal solution to deal with out-of-court disputes, and FIN-NET confirms this.

### **Principle of Mutual Recognition**

13. Regarding the principle of mutual recognition, it has to be recognised that the second banking coordination directive provides for a European passport for credit institutions. According to this directive, all banking activities listed in it and permitted in one Member State should be recognised and could be practised throughout the European Union. According to Article 22 paragraph 5 of the directive, however, Member States are able to impose their national provisions on the basis of protection of the general good. This situation was and remains in some circumstances an obstacle to the achievement of the Single Market for Financial Services. Based on experience so far, mutual recognition stops where contract law (consumer protection regulation applicable to products) starts. In general, EBIC believes that applying mutual recognition in the field of law applicable to consumer contracts would indeed risk affecting consumer confidence as – in a cross-border context – the consumer would require information about consumer protection provision in another Member State, i.e. the home country provisions of the bank. Rather, targeted harmonization (as outlined in section 9 above) should be used as a more effective way to achieving the goals of the single market.

### **Competition and consolidation in the EU**

14. Throughout the expert group reports there is widespread recognition of the importance of promoting competition as a driving force for integration. The banking report also highlights the importance of respecting this “diversity between the providers of banking services in the EU, which appears beneficial to consumers”. Members of EBIC agree on the principle of pluralism in the banking sector provided that there is the same level playing field for all kind of institutions and that there is no distortion of competition. EU legislation should not favour one type of business model or corporate structure or one type of product over another.
15. EBIC would like to highlight that the values of an open market economy and free competition are enshrined in the EU Treaty. European competition policy is built on the view that competition is good for the consumer and industry alike. Over the years, increased competition in the banking sector has stimulated banks positively in a number of ways. They have increased efficiency and cut costs; adjusted business strategies, for example by developing new services and distribution channels; and consolidated through mergers and acquisitions. In

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<sup>3</sup> Green Paper on Alternative Dispute Resolutions, COM (2002) 196 final, 19 April 2002, where the Commission requests feedback as to whether the structure, composition, set-up and functioning of ADRs should be harmonised at the European level (responsible DG: JAI).

addition, increased competition has provided consumers with a wider variety of innovative products at competitive prices from a range of different providers, and has thus contributed to increased economic growth in Europe.

16. So far, consolidation of activities has been seen mainly in wholesale banking services such as corporate bond and equity issuance, and mainly within national boundaries or in defined geographic regions such as in the Nordic-Baltic area.
17. The low level of cross-border consolidation partly reflects legal and regulatory differences, such as consumer and competition policies, which make it difficult to develop a pan-European product range. The banking report states that there are natural, or what it calls “idiosyncratic” barriers to integration, “such as the specificities of local or regional demand and needs, as well as cultural and language barriers”. These facts and market conditions are limiting the extent of consolidation in European financial services.
18. In this context, the full benefits of competition are not always achieved in practice.
  - Decisions of the European Commission have in the past made the case for bank mergers in small countries less attractive (assets sell-off), on the basis of a narrow definition of “national market”. This has in effect prevented banks in those countries from building a capital base large enough to compete at EU level. But the EU and national authorities also have a role to play. The enlightened application of competition rules should allow the financial services industry to consolidate in a beneficial way for both EU and domestic economies. It should be noted however that further consolidation in already highly concentrated domestic banking markets could potentially be damaging for competition and thus detrimental for consumers.
  - An increasingly “functional” approach to EU-legislation leads to a situation where more and more entities are given the opportunity to provide banking services conditional on a supervisory regime that is lighter than those of credit institutions (i.e: plans of the European Commission to allow telecom operators to provide payment services). EBIC therefore believes that the principle of “same business, same risks, same rules” should apply. This would not only help to ensure a level playing field, but would also assure equal treatment in terms of costs.

### **Competitiveness of EU vis-à-vis the rest of the world**

19. In a globalised world, the creation of a European Single Market for financial services is not an end, but rather a means to increasing the international competitiveness of European financial markets. Achieving both a Single Market for financial services and the competitiveness of the EU vis-à-vis global markets involves a difficult balance.
20. Recent research on the competitiveness of nations (IMD World Competitiveness Yearbook 2003) has led to the conclusion that market access (openness) is one of the most important factors for improving a region’s competitiveness. Open markets foster competition, thereby increasing quality and reducing prices for consumers while at the same time giving firms incentives to innovate.
21. Unless proposed regulations and standards undergo a competitiveness test, the prospects of the EU meeting the Lisbon objective of becoming the most competitive economy in the world by 2010 will be much diminished. Systematic assessments of the business impact of EU regulation should therefore be undertaken.

## **2. Effectiveness of the current EU legislative framework and arrangements for supervisory cooperation (Lamfalussy Process).**

22. While Level 3 of the Lamfalussy approach has yet to be put to the test, EBIC is confident of the ability of the Level 3 Committees to contribute to the consistent implementation of European Directives and to the convergence of Member States' supervisory practices throughout the Community, and supports the European Parliament rights to call back implementing measures. Further, EBIC welcomes the establishment of a working relationship with CEBS (in particular the appointment of two EBIC representatives to the CEBS Consultative Panel).
23. However, for the Single Market to become a reality, the Level 3 Committees will need to develop an EU-centric view of policy and promote a culture of co-operation between their members (including an exchange of information). To this end, enhanced supervisory cooperation could be supplemented by mandatory supervisory disclosure. Revealing inappropriate supervisory practices, disclosure could be an efficient tool to increase the convergence of supervisory practices.
24. It is of fundamental importance in the context of the Lamfalussy procedure to establish a clear borderline between the scopes of the levels 1 and 2 and of the levels 2 and 3 respectively. More specifically, the level 3 of the Lamfalussy process being related to the consistent application of European texts, decisions taken at this level should not interfere with texts drafted following the "European" level 1 and 2 processes; level 3 should not serve to set new legislation.
25. We also believe that the level 3 committees should not propose level 3 guidelines or recommendations in areas not covered by the EU legislation, as this would create pan-European standards without following the appropriate existing European legislative procedures. Against this background, we believe that should the level 3 Committees feel that there is a need to develop new regulatory guidance in the areas not covered by EU legislation, then they should submit the case to the Commission, which may in turn develop the adequate level 1 provisions. This would be consistent with the EU framework, which grants the Commission the monopoly of initiative. Furthermore, it would ensure that the Commission retains the responsibility to guarantee the consistency of all the provisions applying on a pan-European basis in the financial services sector. EBIC believes that level 3 Committees should not predetermine policies in areas where EU legislation might be upcoming (e.g. where a debate on a possible Level 1 measure has been or will be launched by the Commission through a Communication or any similar tool of debate)
26. EBIC furthermore believes that debates which have been led at level 1 should not be re-opened at level 2. Rather, level 2 should work within the framework laid down at level 1 and fine-tune or fill the level 1 framework in a meaningful way to facilitate convergent implementation.
27. EBIC would finally like to emphasize that relevant political and strategic decisions must be taken at level 1, while at the same time too prescriptive and detailed drafting should be avoided at this stage.

### **3. General principles and methodology for identifying and prioritising further EU level legislative actions and for improving the EU financial rule-making process**

#### **GENERAL PRINCIPLES**

EBIC would like to present the following list of key principles which should ideally be applied:

#### **Industry consultation**

28. To ensure policy is relevant, European as well as international policy makers need to consult industry and, additionally, should obtain evidence from other relevant sources (including investors, regulators, academic experts) to support decisions about: whether a policy need exists, and if so, the nature thereof; if (and only if) a need exists, what policy approaches might be appropriate; which of the possible policy approaches should be preferred.
29. Making wide and representative industry consultation a standard part of the legislative decision-making process will promote better and more effective legislation, and improve the transparency of policy-making. Consultation should be on the detailed drafting of directives and regulations as well as on the principles. Observing this with the original draft of the Consumer Credit Directive, for example, would have prevented some of the more obvious problems that the original draft has created.
30. If consultation is to be a valuable process for all parties, it must be “real”. There is little benefit in undertaking consultation if decisions have effectively already been taken. In addition, consultations should be carried out in an open, transparent and systematic way. High consultation standards are also required from standard setters. Finally, the timeframe of consultation should be adequate and realistic.
31. At the international level, the consultation by the Basel Committee on Banking Supervision was conducted in an exemplary manner which set very high standards to be aspired to by other international standard setters such as the IASB.

#### **Business impact analysis**

32. The introduction of new legislation should be strictly assessed on the basis of business impact analyses which could be measured by using such tools as proportionality tests and/or cost benefit analyses. It should furthermore be clear and unambiguous in its wording. EBIC further supports the publication of guidance by the Commission on how certain provisions of Directives should be implemented in order to avoid possible misinterpretations thereof.
33. The important objective of a Single Market in financial services, should, however, not be pursued without regard to the balance of costs and benefits of removing barriers. A theoretically perfect Single Market should not be pursued at all costs. A comprehensive analysis of the relevant existing legislative framework should be an important prerequisite in designing regulation for the European banking market.

### **Quality over speed**

34. Where regulation at European level is pursued, quality must prevail over speed. Effectiveness must not be sacrificed in order to meet politically inspired deadlines. A political commitment to the delivery of Single Market objectives must encompass better, more effective and proportionate regulation. Rushed legislation is unlikely to achieve this and risks falling short of the objectives set for it.

### **Subsidiarity**

35. The principle of subsidiarity needs to be respected.

### **Proportionate regulation**

36. Where regulation at European level is appropriate, it must be both effective and proportionate. This applies not only to Directives and Regulations, but also to implementing measures and core standards which result from supervisory cooperation. Proportionate regulation shouldn't favour one type of business model or corporate structure or one type of product over another.

### **All sizes and structures, “same business, same risks, same rules”**

37. Financial regulation should be designed for credit institutions of all sizes and structures. It should follow the principle of “same business, same risks, same rules”.

### **Coherent Implementation and enforcement**

38. The mindset of the regulator needs to change: having just completed the legislative part of the FSAP, rather than presenting new legislative measures, European regulators should now focus on implementation and enforcement. Consistent interpretation and application of the FSAP measures (i.e., in a Lamfalussy context, Level 3) and effective enforcement thereof (i.e., in a Lamfalussy context, Level 4) will greatly determine whether or not a Single Market for financial services has been created in the EU. EBIC would therefore appeal to the European Commission to live up to its role as guardian of the Treaties by putting in place the adequate mechanisms to monitor and enforce proper implementation at Member State level. As the EU expands this will be of increasing importance. Against this background, EBIC would recommend that the appropriate resources - at either Commission or Member State level - be allocated for the purposes of monitoring and meeting compliance requirements on a timely basis.
39. EBIC feels it is essential that all efforts be made at the European level to ensure coherent implementation and interpretation of EU legislation by member countries. Striving for such improvements at the national level is essential for the credibility and acceptability of EU legislation and to create a true level playing field. The Lamfalussy level 3 committees have an important role to play in this respect and EBIC is keen to assist them in this task. Similarly, inconsistencies in EU legislation must be eliminated, for example.

## **RULE MAKING**

### **Type of regulation: Self-regulation as an alternative to binding regulation**

40. EBIC welcomes the banking report's recognition that "self regulation can be a flexible and powerful instrument" as well as the report's general support to using the most appropriate instrument for each policy objective. Indeed, EBIC believes that part of the consultation exercise should be to assess on a case-by-case basis what type of regulation would serve as the best tool to achieve a particular outcome if there is a perceived need for action. Various regulatory options exist that range from self-regulatory methods to binding regulation, and the different types should be given equal consideration in discussions on devising regulatory solutions to European problems.
  
41. In considering the case for expanding the use of banking self-regulation in the EU, one must have regard to definitions; the advantages and disadvantages of self-regulation; and the prerequisites for the effectiveness of self-regulation (see Annex 2 for details).

#### **4. Supervisory convergence and enforcement**

42. The importance of consistent interpretation and application of regulatory and supervisory requirements has already been noted in this paper. The delivery of these objectives will in part be determined by whether or not the appropriate structures are in place to encourage supervisors to cooperate. This was recognised by the Expert Group on Banking in its call to improve the way that cross border supervision of institutions is organised today. EBIC agrees with the Expert Group's conclusions and feels strongly that inconsistent application of supervisory requirements across jurisdictions results in significant cost and duplication of effort for internationally active banks.
43. EBIC welcomes the European Commission's recognition of the need for improvements. The development of the established role of the consolidating supervisor in the proposed Regulatory Capital Directive will make an important contribution to avoiding unnecessary duplication and costs, whilst enhancing supervisory cooperation. The Commission's approach respects the role of national supervisory authorities whilst ensuring that a group based in the European Union need only submit an application (e.g. to adopt the Internal Ratings Based Approach for credit risk) to the consolidating supervisor. It encourages cooperation by encouraging supervisors to work in full consultation when determining applications. Importantly, the Commission's approach gives supervisors 6 months to reach an agreed view after which the consolidating supervisor can take its own view on the application.
44. Convergence of supervisory approaches would be further promoted by ensuring that supervisors have a common set of supervisory tools at their disposal. It would also be promoted by the introduction of adequate supervisory disclosure. EBIC therefore welcomes the inclusion in the proposed Regulatory Capital Directive of a requirement for supervisors to disclose information to enable a meaningful comparison of approaches adopted across the EU.
45. The latest Internal Market scoreboards published by the Commission indicate a growing implementation deficit in various Member States. The newly energised approach of the Commission to enforcement of EU measures, together with commitment from all interests parties, including the industry, will be critical to the consistent implementation of both the letter and spirit of FSAP rules and therefore to the FSAP's success. EBIC has welcomed the regular publication of the Commission of FSAP Progress Reports. Such reports should continue beyond 2005 and take the form of specific scoreboards of Member States' performance in terms of implementing and enforcing FSAP rules.

## **5. Specific issues identified for further attention by EU policy-makers**

### **Fiscal barriers**

46. In recent years, the range of financial services available to businesses and consumers has vastly expanded. Financial markets have become much more competitive. In order to stay competitive and to be able to cope with the burden and cost of rapidly changing information technology and increased shareholder pressure for financial performance, financial groups have been obliged to seek structural cost savings and exploit synergies by integrating, centralizing and rationalizing their functions internally and by outsourcing to third parties (e.g. cross-selling of financial products and centralized production of IT and other support services). As a result of this integration and centralization of functions and as a result of the obligation to comply with transfer pricing regulations, the amount of intra-group cross-border supplies and cost allocations has increased dramatically in the financial services industry.
47. With that in mind, EBIC is of the view that fiscal barriers are among the biggest obstacles to integration in European financial markets and that the Commission and member states should continue their work to abolish them. EBIC would fully support the Commission in any actions to tackle the fiscal obstacles identified in the report (Box 7 page 19 in the banking report) and listed under recommendation for action 7. EBIC supports the recommendations of the banking expert group that as a first step the European Commission is requested to carry out a study identifying precise areas of and the cost of tax discrimination. Some potential areas for inclusion in this study are shown in Annex 3 of this paper.

### **Payments**

48. EC policy for payments should consist of a combination of measures, both based on legislation and self-regulation. The industry within the European Payments Council (EPC) is working towards the creation of SEPA, the Single Euro Payment Area. Community legislation is only desirable to remove legal obstacles that prevent the creation of EU-wide market conventions and agreements, and/or where a clear threat to consumers can be evidenced. Conversely, self-regulation can play a more effective role, e.g. in areas where market practices are crucial to the attainment of the objectives, for example: execution times, value dates, customer mobility, agreement on technical standards, revocability rules, etc.

## **6. (Aspects divergent from/or in addition to the expert groups' reports)**

### **Systemic Risk**

49. The expansion of banking and financial groups and their growing involvement in increasingly integrated European securities markets are also affecting the likelihood that disturbances originating or channelled through capital markets will expand beyond national borders. EBIC therefore appreciates the idea of the Financial Services Committee that supervisors, central banks and finance ministries work together to ensure that appropriate plans and mechanisms are in place to respond to any developing financial crisis, which threatens the stability of the financial system.

### **A stronger EU voice at international level**

50. The development of technology has led to an unprecedented globalisation of the financial sector. Confidence in the global system is the corner stone of further development. It is of utmost importance to promote confidence of investors and depositors as well as confidence in inter-bank relationships. EU positions should be defended efficiently when developing, common standards for all players/market participants, in particular in areas such as capital adequacy, money laundering, fight against terrorism financing, data protection and accounting standards.
51. There are international bodies that provide guidance on a number of these issues (Basel Committee for Banking Supervision, IOSCO, FATF, IASB, etc.). Given the fact that the European Commission/Union is not always a full member of these international bodies, but rather (some) Member States of the EU, does clearly not facilitate the representation of European interests in these fora. In certain cases, this may affect the ability of the EU to influence the content of international standards and therefore be contrary to European interests. Due to the different nature and role of these fora, ad hoc solutions between European “participants/members” should be preferred over a one-size-fits-all approach. Possible solutions may include inter alia a strengthening of the role of the Commission, and, in the accounting field, of EFRAG. Once they are firmly established and have developed a balanced European view of policy, the Level 3 Committees (CESR, CEBS and CEIOPS) might also play a role in some of these bodies (e.g. CESR in IOSCO).
52. The EU should develop a stronger voice at international level to influence the outcome of the deliberations on international standards.
53. To ensure consistency and avoid overlap EBIC recommends closer liaison between international standard setting bodies on inter-related matters. For example, regular meetings between the Basel Committee on Banking Supervision and the IASB.
54. Convergent accounting standards play a vital role in global markets, allowing financing decisions to be taken on the basis of agreed standards. However, increased efforts need to be taken to ensure that the standards adopted at the global level meet the needs and requirements of the European Union's banking industry (IAS 32 and IAS 39).

55. In conclusion, EBIC believes that international standards should be integrated into European legislation in a way that is not only consistent with the remaining “acquis communautaire”, but also ensures a degree of democratic accountability. International standards should therefore be evaluated on a case-by-case basis.
56. The importance of the transatlantic relationship for both the EU and the US cannot be underestimated and EBIC welcomes the role played by the Commission in the EU-US financial markets regulatory dialogue. The concept of regulatory equivalence is at the core of this dialogue and requires extensive EU-US cooperation and convergence on common principles.
57. Similar structured dialogues should be established with other main EU partners.

### **Action Plan Corporate Governance**

58. The Commission’s Action Plan for “Modernising Company Law and Enhancing Corporate Governance in the European Union” should give further impetus to a reform of company and capital market law and accounting rules in the EU, as far as listed companies are concerned. The recent scandals affecting corporate Europe have attracted negative publicity and undermined investor confidence. The implementation of the Plan, adjusted to take account of the lessons learned from the recent affairs, should therefore be a priority.
59. EBIC welcomes the measured approach taken by the Commission since December 2003 and sees no immediate need for legislative initiatives other than those already contemplated in the Plan. EBIC calls for effective coordination of the national responses to the accounting regulatory issues highlighted by the recent scandals. Many Member States are currently adopting national measures to restore confidence in their country as a financial market place. Yet, cross-border cooperation is essential if Europe is to make sustainable improvements in the accounting industry and maintain investor confidence.

### **Anti-Money Laundering**

60. The fight against money laundering and terrorism financing remains a major issue which shall be closely followed at international level. With the future adoption of a new Directive on Money Laundering and a Regulation on payer’s information accompanying credit transfers, the European Union will have implemented the international standards in this field (e.g. the revised FATF forty recommendations as well as the special recommendations on terrorist financing). EU legislation in the interconnected areas of anti-money laundering, payments and terrorist financing should be properly coordinated and coherent.

## **ANNEX 1: General ambitions for the further development of a single financial market**

**Definition of the consumer:** EBIC believes that the definition of a consumer as “*a natural person acting for purposes which can be regarded as outside his trade or profession*” should not only be identical throughout all European legislative texts, but – more importantly – should be implemented identically throughout Europe. European consumer protection rules can only be efficient if they are addressed to the same addressees all over Europe;

**Pre-contractual information requirements:** EBIC strongly believes that the issue of “information overload” needs to be addressed in this context: There should be less pre-contractual information and the information requirements should be more consistent across directives. EBIC would therefore recommend the establishment of a uniform list of appropriate pre-contractual information, which should apply to all EU consumer protection directives in the financial services area. In order to enable a consumer to compare offers and to make an informed decision – especially in a cross-border environment - Member States should refrain from keeping or introducing additional requirements other than the ones listed below:

- Basic information on the supplier (complete identification and contact details);
- The (final) price the consumer will pay to the bank;
- The main attributes of the product or service offered;
- Important contractual conditions such as the existence of a right of withdrawal or reflection period and the duration of the terms announced in the offer/advertisement;
- Early repayment terms (if any);
- Minimum fixed time period of commitment binding the consumer to the contract, if any, and conditions to give notice for cancellation;
- All relevant information should be provided in a durable medium.

Whether or not the use of ESIS is a valuable tool to achieve the above mentioned objective, and under what conditions it could be used in the perspective of this desirable harmonisation of pre-contractual information, should be analysed on a case-by-case basis in full consultation with the stakeholders.

While the described basic set of pre-contractual information should in general be given for all products/services, EBIC would like to present some examples where flexibility should be applied:

- ⇒ On the one hand, exemptions should be foreseen for very specific products i.e. banks should not be requested to provide the complete list of information for a revolving credit at each interval.
- ⇒ On the other hand, this basic list of information might need to be complemented by additional binding pre-contractual information for specific, more sophisticated products (e.g. investment or pension fund product).

**APRC:** EBIC feels that a single APRC including exclusively those costs levied by the lender for his benefit should be introduced as this is the only way to provide a useful and consistent means of comparison for consumers.

**Right of withdrawal:** EBIC would recommend the development of a uniform set of rules concerning the right of withdrawal along the following lines:

- ⇒ Principle: a common and uniform time period of 7 working days should be established for any consumer contracts for practical and legal certainty reasons at the EU level.
- ⇒ Exceptions: exceptions to this general principle would need to be made for the following reasons:
  - Contracts involving a market risk or price and/or capital market fluctuations, such as foreign exchange, money market instruments, transferable securities, units in collective investment undertakings, financial future contracts including equivalent cash-settled instruments, forward interest-rate agreements (FRAs), interest-rate, currency and equity swaps and options to acquire or dispose any instrument referred to in this list of exemptions.
  - If the consumer has received full advice. For instance, as is the case with contracts concluded before a notary, court or other similar public authority entrusted to guarantee that the consumer has received all information required.
  - In the case of an opt-out possibility/or reduction of the withdrawal period, as long as the consumer is properly advised about the consequences of these provisions (crédit lié)
  - If there exists a pre-contractual right of reflection in national legislation. In this case, the bank should not be obliged to provide the consumer with a post-contractual right of withdrawal.
- ⇒ Need for a general stop/end date : Directive 85/577/ EEC on the Protection of the Consumer in respect of Contracts negotiated away from the business premises, as well as Directive 2002/65/EC on Distance Marketing of Financial Services do not provide for any stop/end date of the withdrawal period. Equally, the proposed draft for the revision of the consumer credit directive does not contain a stop/end-date. The right to withdraw from an agreement for an ‘unlimited period’ leads to an unacceptable situation of legal incertitude for any supplier of goods and services and it could also result in an increase of prices to cover the risk of eventual abuses in using the right of withdrawal. Against this background, the introduction of an end-date, as contained in the general distance marketing directive<sup>4</sup>, seems indispensable from the point of view of EBIC.

In any case, EBIC recommends that a uniform set of provisions on the right of withdrawal along the lines described above should be developed at the EU level and uniformly enforced throughout the EU at the national level.

EBIC has already expressed its view on the right of withdrawal in the context of its comments on the CCD and we attach this letter for your further information (in particular, see our comments on article 11.3 in paragraph E, p.25).

**Harmonising rules for on-line identification and authentication:** Opening of (cross-border) on-line accounts over the internet should be made considerably easier. This should be achieved by enforcing existing legislation (the Electronic Signatures Directive) and by establishing harmonised rules for identification and authentication, while respecting the technical options on identification

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<sup>4</sup> Article 6 of the Directive 97/7/EC on the protection of consumers in respect of distance contracts provides a three months stop/end date of withdrawal period (Art. 6, para. 1: "...if the supplier has failed to fulfil the obligations laid down in Article 5, the period shall be three months").

standards that Member States may choose to explore (“uniform rules, not uniform solutions”, i.e. technological neutrality). At present, the procedure customers have to follow to provide proof of identity varies from one Member State to another, but is always a cumbersome and distinctly “off-line” exercise. This time-consuming and costly procedure could be avoided if the EU established a legal basis explicitly permitting accounts to be opened throughout the EU with a qualified electronic signature. This would provide the banks with the legal certainty they need.

**Interdiction of contracting on-line:** Some Member States do not allow guarantee agreements or consumer loan contracts to be concluded over the internet, but explicitly prohibit such contracts being concluded “in electronic form”. In other Member States e-contracting is permitted. This situation results in distortion of competition and is detrimental to banks operating in Member States where e-contracting is prohibited. EBIC believes that there is no good reason to prohibit consumer loan agreements being concluded over the internet: the right of withdrawal foreseen in the Directive on Distance Marketing of Financial Services provides consumers with an adequate level of protection.

**Mutual recognition of ‘KYC’ standards:** The second Money Laundering Directive’s ‘Know Your Customer’ rules are sometimes interpreted very restrictively by competent authorities in Member States, requiring for instance the submission of certain documents usually required for domestic identification purposes and therefore making it impossible for consumers from certain Member States to open an account. The aforementioned requirements set by the supervisory authorities constitute an obstacle to cross-border business relations. This situation could be remedied by a mutual recognition of the equivalence of national KYC standards in the EU. In this context, EBIC welcomes the Commission's intention to allow a mutual recognition of KYC standards within the EU, as provided for in Article 15 of the proposal for a Third Money Laundering Directive.



## European Banking Industry Committee

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European Banking Federation (EBF) • European Savings Banks Group (ESBG) • European Association of Cooperative Banks (EACB) European Mortgage Federation (EMF) • European Federation of Building Societies (EFBS)  
European Federation of Finance House Associations (Eurofinas)/European Federation of Leasing Company Associations (Leaseurope)  
European Association of Public Banks (EAPB)

Commissioner David BYRNE  
European Commissioner Health  
and Consumer Protection  
European Commission,  
B 1049 Brussels

18 June 2004

Dear Commissioner Byrne,

We would like to thank the Commission for the time to debate the emerging issues around the Consumer Credit Directive, following the vote in the European Parliament plenary session (1<sup>st</sup> Reading) at the end of April. We very much welcome your philosophy of stakeholder participation during this part of the law making process and as such, we hope that this letter continues to build on our opening dialogue.

As part of our role to allow market participants to provide advice and ensure a representative and coordinated industry view on the key issues facing the industry, we are keen to ensure that the Directive creates a legal framework that is both protective of consumers and conducive to an innovative and inclusive market for consumer credit. Whilst we feel that the vote in plenary moved the file closer to this aim, it nonetheless gave rise to a text which could be further finessed to the benefit of both lenders and consumers alike.

It is in this vein that we have attached a number of short papers to answer the questions raised at our meeting and outline the rationale for our position on certain other aspects of the Directive which we feel are key, including:

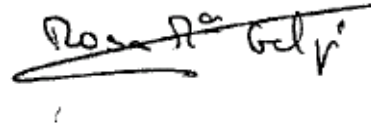
- A. Scope
- B. Responsible lending and responsible borrowing. Duty to advise
- C. Cumulative sets of pre-contractual information. Risk of inconsistencies
- D. Duty to inform consumers/Databases
- E. Right of withdrawal
- F. Linked Credit Agreements
- G. Early repayment
- H. Credit intermediaries
- I. Annual Percentage Rate of Charge (APRC)  
Annex: Calculation of the APRC

Naturally, some of the issues raised are complex and technical and we would be happy to explain them more fully with your team if this would be beneficial to you. To this end, we will ask our secretariat to contact you shortly to ascertain where the EBIC working party might best assist.

Yours sincerely



Ian Mullen  
EBIC Chairman



Rosa Maria Gelpi  
Chairwoman EBIC Working Group CCD

## **A. Scope of the Consumer Credit Directive**

### **1. Exclusion of home loans and all mortgage loans, Art.3-2-a**

The EBIC feels that the text of the Directive should concentrate on credit granted to consumers for consumption by clearly differentiating between consumer credit and mortgage credit, whether secured by a mortgage on real property or by an equivalent surety.

EBIC therefore very much welcomes the exclusion of Home Loans from the scope of the Directive. For the sake of consistency, we understand that Real Estate Loans ancillary to Home Loans (as widely used in France where the definition of Home Loans is exclusively based on the purpose of the loan instead of the surety) are equally excluded from the scope of the Directive.

EBIC however considers that all mortgage loans including Mortgage Withdrawal / Equity Release Loans (mortgage loans taken out for consumption purposes), should be excluded from the scope of the Directive.

There are two main reasons for this further exclusion:

- Mortgage Withdrawal/ERL, being mortgage loans even if taken out for consumption purposes, do not fit into a legal framework specifically designed to address consumer credit products. Indeed, mortgage loans are different, long-term products, often funded through long-term instruments, such as mortgage bonds and mortgage backed securities (MBS), with a low risk profile and low interest rates. Therefore, typical consumer credit provisions, such as the right of withdrawal and prepayment rules are not compatible with mortgage credit.
- All types of mortgage loans, including Mortgage Withdrawal/ERL, should be subject to one single set of rules:

It would be incongruous to have one category of loans, i.e. mortgage loans, split between two types of rules, the Code of Conduct on Home Loans or the Consumer Credit Directive depending on their purpose. This would be confusing for lenders as well as for consumers, especially in the case of mixed loans (combining both housing and consumption purposes), where one single loan could fall under the two different sets of rules. As such, it would lead to an increased risk of litigation. Indeed, it should be recalled that mortgage loans have a decisive common denominator: the borrower secures his loan against his home in return for a lower rate.

Neither would a split between two sets of rules be workable. Indeed, considering Member States' legislation, it appears that in a number of countries (Denmark, Germany, Ireland, the Netherlands, Austria and the UK, the purpose is not considered in the legislation and is therefore not even known by the lender. This means that any loan secured on a property (including mortgage withdrawal / ERL) is necessarily considered and regulated as a mortgage loan, without regard to the purpose. Any regulatory difference made on the basis of purpose would therefore be impossible to apply in practice in these Member States. Mortgage loans should consequently be defined and classified on the basis of the mortgage surety, which is the only workable criterion.

There are also practical reasons for excluding mortgage loans from the scope of the Consumer Credit Directive. Indeed, a number of initiatives are currently outstanding,

which aim to both achieve an Internal Market for Mortgage Credit and improve the implementation and working of the Code of Conduct for Home Loans adopted in March 2001:

- At the Commission level, the Forum Group on Mortgage Credit launched in March 2003 is currently:
  - Assessing how to achieve an Internal Market for Mortgage Credit. To this end, the Forum Group is in the process of identifying obstacles and preparing policy recommendations.
  - Assessing the implementation of the Code of Conduct in a threefold perspective: content, status and uptake. The industry and the Commission are discussing the possibilities of improvement and preparing concrete recommendations to this end.

The final report of the Forum group is expected by September 2004. Based on these discussions and resulting recommendations, the Commission is to take position and present its own conclusions by the end of 2004.

- Within EBIC, there are ongoing pan-industry discussions on possible improvements to the Code to:
  - Ensure that the European Code of Conduct continues to be applied and that its application is further improved by credit institutions in most of the EU Member States, including the new ones;
  - Provide consumers with a European harmonized and standardized set of information on Home Loans, guaranteed at a high level.

In this context, the EBIC believes that no decision or measure can or should be taken concerning the field of mortgage credit as long as the Forum Group and the Commission have still to complete their work and present their conclusions. Any other step would amount to a strong disincentive to implement the Code of Conduct, especially in the new Member States.

## **2. Small amount credits, Art. 3-2-a**

EBIC considers that the threshold of 500 Euros must be maintained. The management of small amount credits is very expensive. If credits of below 500 Euros were subject to the detailed provisions of the CCD, they would either become too expensive or unprofitable; they simply would no longer be made available. Small amount credits are closer to “payment facilities” than to “credits”. They could however be covered by the terms of Art. 4-a (new) on preliminary information, signed and submitted in writing to the parties.

## **3. Overdrafts, Art. 6-a (new)**

Consumers’ interests will be better protected by appropriately applying to overdrafts and advances on current accounts only certain elements of the CCD rather than the full set of provisions. Overdrafts and advances on current accounts are long established and well understood products valued for their simplicity and low cost. The partial application of the directive’s provisions, as voted by the European Parliament, preserves this useful financial tool.

#### **4. Exclusion of surety agreements, Art. 23-2-1**

The EP has proposed -in amendment 47- to limit the scope of the directive to credit agreements (instead of credit agreements and surety agreements). The Commission has indicated it cannot support this amendment. However, we believe the amendment of the EP is justly made. First of all, the necessity to include surety agreements within the scope of the directive is not sufficiently demonstrated. We haven't received proof that national provisions on surety agreements are inefficient. Furthermore, the objectives of the directive do not demand an inclusion of surety agreements. Besides, a directive on consumer credit is not the place to regulate surety agreements extensively.

In case surety agreements were nevertheless to be included in the directive, we would like to make the following observations:

The Commission's text, pursuant to which "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" does not take in due consideration the practice - common in many Member States - of guarantees being given by close relatives of the borrower.

Thus, these guarantors are well aware of the consumer's economic situation well in advance of the three months deadline; if creditors are obliged to wait for three months after the consumer's default in order to take orderly safeguard measures against the guarantor:

- Guarantors acting in bad faith will use this extensive time period in order to alienate assets.

Whereas,

- Guarantors acting in good faith will see their interests harmed, because they may have to pay three months' extra interest charges.

Moreover, from a policy point of view, the provisions governing the guarantee and the guarantor's benefit of discussion<sup>5</sup> are integral part of the contract law of Member States. If there is a need to review them, a more long-term procedure, involving law experts and academia, such as the Commission's "European Contract Law" project<sup>6</sup> is required.

Thus EBIC would urge the Commission not to include Art. 23-2-1 in the modified proposal.

#### **B. Responsible lending and borrowing, Art. 6-1. Duty to advise, Art. 6-3**

##### **Responsible lending and borrowing**

We welcome the acknowledgement in the EP amendments that both parties to the credit agreement should behave responsibly. In order to have a truly reciprocal duty and a real balance between the contractual rights and obligations of the parties we believe that the consumer (and guarantor) must be expected to reply accurately and in full to the creditor's request for information, providing any

<sup>5</sup> DA beneficium ordinis; DE Einrede der Vorausklage; EL δικήσεως ευεργέτημα, ένσταση της δικήσεως; EN right to object, benefit of discussion; ES beneficio de excusión; FR bénéfice de discussion; IT beneficio di escussione; NL voorrecht van uitwinning; FI esikanne-etu; SV beneficium ordinis.

<sup>6</sup> See COM(2003) 68 Final Communication from the Commission to the European Parliament and the Council: a More Coherent European Contract Law - An Action Plan.

relevant information potentially capable of affecting the latter's ability to accurately assess the former's financial situation and ability to repay.

### **Duty to advise**

Article 6-3 contains in its present form a duty to advise for creditors and - where applicable- credit intermediaries. We believe this provision may have grave and far-reaching side effects, perhaps unthought-of by its drafters. In fact, the obligation for the creditor or the credit intermediary to seek to establish the best type of credit for the consumer removes the consumer's responsibility and transfers it to the creditor. In order to maintain the balance between the parties this paragraph should be deleted, in the same way as recital 15 was deleted.

What is more, a person providing advice could, under national law, be responsible for the results of the provision. Some consumers could use this Article as a pretext for refusing to repay their loans, challenging the validity of their credit agreement. Art. 6-3 could become a source of litigation. Facing this grave prospect, credit institutions might:

- o Increase customer rates to protect profit margins.
  - o Credits becoming more expensive and more difficult to obtain, this will end up with exclusion of a certain group of "poor" consumers.
- Providing advice as stipulated may create conflicts of interest

The Commission proposal (Art. 6-3) would oblige the credit institution to take into account, in offering advice to the consumer "the advantages and disadvantages associated with the product proposed". The creditor must then consider the personal circumstances of the consumer to enable him to decide which features of the product are advantages and which features are disadvantages for that consumer. The result could be different for different consumers. This adds substantially to the burden of the requirement to give advice.

It could also be underlined that:

- Providing advice is not always possible

How can one provide personalised advice in the case of distance selling? The blooming of the new market for distance selling of simple products we are witnessing today may come to a halt if financial institutions feel hesitation and even prohibition of use of channels like the internet for concluding credit agreements .

- Providing advice is not always necessary

If the blooming of internet sales proves one thing, it is that consumers themselves have felt they are able to do away with personal advice. And this is not only the case in distance selling. Why should a consumer feeling knowledgeable and well informed be burdened with a process of personal advice he did not solicit for?

- Advice in most financial markets is an additional service, entailing additional cost

There can be a clear and apparent distinction between merely offering a product and information on products, and offering advice on one or more products. These are two different economic activities and two distinct services. A third party could for instance advise on the products of several other

credit institutions. As opposed to giving information, giving advice to consumers must be thought of as an additional chargeable service (as e.g. is investment advice, offered by banks to investors, who individually seek it and never seriously argue that they should receive it for free). Therefore, the creditor must be able to choose to provide it or not. For his part, the well-informed consumer must be able to choose for a product without being obliged to take advice and take the responsibility of his final choice.

## Conclusion

Balanced approach to responsible lending - Providing advice should not be mandatory.

Lenders' and borrowers' responsibilities should be well balanced. Therefore, we appeal to the EU Commission to reintroduce Art. 6-3 of the JURI vote. A special provision is not necessary, given the general provision concerning responsible lending. Thus, legislators in at least two Member States – Sweden and the Netherlands – have already clearly and consciously chosen against the adoption of a mandatory duty to advise in (the proposal for) the new Financial Services Act; under no circumstance do these acts oblige banks to opine on the “most suited” financial product for a particular customer. We urge the Commission to take this in due consideration.

For the aforementioned reasons we strongly oppose a general duty to advise. If a credit institution provides the consumer with all the information he needs to make an independent and well-informed choice, there is no reason to demand of the credit institution to give personal advice in addition.

## **C. Cumulative sets of pre-contractual information, Art. 4 and Art. 6-2**

Under the adopted Directives on Distance Marketing of Financial Services<sup>7</sup> (DMFS) and the E-Commerce Directive<sup>8</sup> (ECD), as well as under the proposal on Consumer Credit Directive<sup>9</sup> (CCD), the supplier shall provide the consumer with a set of information before the conclusion of a contract. The following wording used in these Directives “before or prior to the conclusion of the contract” actually covers the advertisement and the pre-contractual phase.

While the E-Commerce Directive is a horizontal framework Directive aiming at facilitating the free movement of information society services in the Internal Market, the DMFS Directive focuses on the gradual harmonisation of legal provisions of Member States concerning the distance marketing of consumer financial services. The CCD proposal focuses on a particular financial product, consumer credit.

A consumer credit agreement marketed/advertised and concluded via distance means<sup>10</sup> will in principle be subject to the three Directives according to several provisions, for example:

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<sup>7</sup> Directive 2002/65/EC of 23 September 2002 concerning the distance marketing of consumer financial services and amending Directive 90/619/EC and Directives 97/7/EC.

<sup>8</sup> Directive 2000/31/EC of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market.

<sup>9</sup> Proposal for a Directive on the harmonization of the laws, regulations and administrative provisions of the Member States concerning credit for consumers (2002/0222 COD).

<sup>10</sup> See definition of “distance contract “, Art. 2 letter a) of the DMFS: any contract concerning financial services concluded between a supplier and consumer under an organized distance sales or service-provision scheme run by the supplier, who, for the purpose of that contract, makes exclusive use of one or more means of distance communication up to and including the time at which the contract is concluded.

- Recital 14 of the DMFS “certain financial services are governed by specific provisions of Community legislation<sup>11</sup> which continue to apply to those financial services. However, principles governing the distance marketing of such services should be laid down”;
- Recital 6 of the DMFS : “this Directive should be applied in conformity with the Treaty and with secondary law, including the Directive 2000/31/EC on E-commerce, the latter being applicable solely to the transactions which it covers”;

The following examples of pre-contractual information requirements included in the three different Directives are, on the one hand, found to overlap and leading to possible inconsistencies. On the other hand, duplication or accumulation of information requirements, which is often the case when comparing provisions from the three Directives, might eventually be avoided depending on how Member States decide to transpose the Directives, in particular the DMFS Directive, due to be implemented by all Member States in October 2004.

Against this background, the following non-exhaustive list of examples are meant to highlight some issues which might deserve careful consideration when ensuring consistency and coherent consumer protection rules.

- Duration of the contract

The creditor needs to inform the consumer on the duration of the credit agreement under the CCD (Art. 6, para. 2, letter b). This information is also required in the so-called “infobox” - Art. 4 new “Standard Information” - introduced by the Parliament’s first reading. In addition, under the DMFS, the creditor will also have to inform on the minimum duration of the distance contract in the case of financial service performed permanently or recurrently (Art. 3, para. 1, subpara. 3, letter b). Moreover, the obligation to describe the main characteristics of the financial services normally includes information on the duration of the service (DMFS, Art. 3, para. 1, subpara. 2, letter a).

- Price, total cost of credit

Another example of over-lapping information obligations is found in the information on the total cost of credit: Art. 6, para. 2, letter e) of the CCD requires the creditor to inform on the total cost of credit to the consumer. In addition, the same provision (Art. 6, para. 2, letter d) requires the creditor to inform on recurrent and non-recurrent charges, including additional non-recurrent costs such as taxes, administrative costs, legal fees, etc, which the consumer has to pay on concluding the agreement. The European Parliament’s amendment introducing the “infobox” also requires information on the total cost of the credit. Moreover, Art. 3 para. 1. subpara. 2, letter b) of the DMFS provides an obligation to inform the total price to be paid by the consumer to the supplier, including all related fees, charges and expenses and all taxes paid via the supplier. In addition, Art. 3, para 1. subpara. 2, letter d) of the DMFS also has a requirement to give notice on the possibility that other taxes and/or cost may exist that are not paid via the supplier or imposed by him. Finally, Art. 5, para. 2 of the ECD provides that price information shall clearly and unambiguously indicate prices and in particular, it must indicate whether prices are inclusive of tax and delivery costs.

- Right of Withdrawal

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<sup>11</sup> I.e. The Consumer Credit Directive 87/102/EC, currently under revision.

- o Exercise of the right: Art. 6, para. 2, letter I) of the CCD lays down the creditor's obligation to inform the consumer on the time period during which the latter can exercise his right of withdrawal. In addition, Art. 10, para. 2, letter h) of the CCD requires creditors to inform on the procedure to follow in order to exercise the right of withdrawal. When concluding the same agreement via distance means, the supplier will have to (also) inform on practical instructions for exercising the right of withdrawal (procedures ?), indicating, inter alia, the address to which the notification of withdrawal should be sent (Art. 3, para. 1, subpara. 3, letter d) of the DMFS ). In addition, Art. 3, para. 1, subpara. 3 letter a) of the DMFS also requires the supplier to inform on the existence or absence of this right, as well as the duration and the conditions for exercising it, including the consequences of non-exercise of this right;
- o Start date: Art. 11 of the CCD defines the start date as the date, on which a copy of the executed credit agreement is transmitted to the consumer. Art. 6, para. 1, of the DMFS provides a two-options rule to define the beginning of the withdrawal period; a) either the day of the conclusion of the distance contract (except for life insurance contracts) or b) the day on which the consumer receives the contractual terms and conditions and the information in accordance with Art. 5, para. 1 or para. 2 of the DMFS, if that is later than the date referred to as option a).

- Internal Redress Schemes and ADR's

Art 3. para. 1, subpara. 4, letter a) of the DMFS requires to inform on the existence of ADR's and methods for having access to them. Art. 10, para. 1, subpara. 3 of the CCD provides that credit agreements shall mention the existence or not of ADR's. Should they exist, information on procedures to access to them should be also provided.

- Commercial Communications and marketing approach

Before or at the same time a supplier and a creditor are in a position to provide pre-contractual information (a creditor is not necessarily also a supplier of goods/ services) they might need to address commercial communications to interested or potentially interested consumers. How to approach consumers with a view to conclude distance contracts of financial services is also not clear.

The general legal regime for unsolicited commercial communications via electronic means is regulated under Art. 7 of the ECD. This provision leaves it to Member States to decide freely to permit or ban unsolicited commercial communications under certain conditions (opt-in or opt-out regime). Art. 10 of the DMFS Directive lays down different rules concerning unsolicited commercial communications depending on the marketing means used by the supplier; automated calling systems and fax machines are subject to an opt-in system while any other means (i.e. electronic means envisaged by the ECD) are subject to the free choice of the Member States.

Moreover, Art. 7 of the ECD provides that in addition, in those Member States where unsolicited commercial communications (via e-mail) are permitted, suppliers shall be clearly and unambiguously identified (nothing new, as this is also requested under the general information obligations provided in Art. 5 of the ECD).

#### **D. Duty to inform consumers/ Databases, Art. 8-2**

The obligation to inform the consumer and, where appropriate, the guarantor of the result of any consultation of a central database, does not improve the protection of most consumers; on the contrary, it is an added cost. This information should be provided “on request”, as laid down in the EU Commission’s original Proposal.

#### **E. Right of withdrawal, Art. 11-3**

EBIC is strongly in favour of the European Parliament's clarification of Art. 11-3 and in particular the abolition of the borrower's option to return the product purchased using credit to the lender during the withdrawal period.

However, EBIC is still very concerned about the proposed right of withdrawal regime and in particular the consequences of extending the withdrawal period to 14 days.

- EBIC would like to call the European Commission's attention to the fact that the concept of "right of withdrawal" does not have the same consequences throughout Europe:
  - In certain Member States, the right of withdrawal allows the borrower to pay back to the lender the amount made available under the credit contract.
  - In other Member States, the right of withdrawal prevents the lender from making the credit available to the borrower during the withdrawal period. Although this is referred to as a "withdrawal right", it is in effect more of a right of reflection.

It appears that the European Commission prefers a model that enables consumers to use the sum borrowed as soon as the contract is concluded. If the consumer wishes to withdraw from the agreement, he or she must repay the lender, using any means at his or her disposal, including credit obtained at more advantageous terms from another credit institution.

EBIC notes that the way in which Art. 11 is drafted will not enable uniform transposition throughout the European Union. Not only does Art. 11 fail to expressly stipulate that the sum borrowed may be made immediately available to the borrower, but the EU Parliament also voted against full harmonisation of the right of withdrawal.

Under these conditions, national regulations that prevent borrowed sums from being made available during the withdrawal period could be maintained. In these countries, consumers will have to wait 14 days before having the money that will enable them to make the purchase they chose to finance by credit. This excessively long period is against everyone's interests:

- Consumers, instead of being protected, will see their plans complicated and possibly jeopardized.
- Lenders involved in cross-border transactions will be at a serious competitive disadvantage with respect to credit institutions based in Member States whose regulations enable credit to be made available immediately.
- Suppliers will have to wait 14 days before making a credit sale.

- EBIC believes the proposed legislation may be improved in four ways:
  - Generally speaking, the exercise of the right of withdrawal should be fully harmonised at the European level. EBIC asks the European Commission to make its model more explicit by expressly allowing lenders to make credit available to borrowers before the end of a 7-day withdrawal period for all types of credit (as already fixed in the framework Directive on Distance contracts 97/7 instead of the 14-day period proposed in the CCD) and to make sure that certain Member States will not be able to continue to prevent credit from being made available during the withdrawal period, to the detriment of consumers, lenders and suppliers of goods and services. On explicit request of the consumer in writing, he should be allowed to waive his right of withdrawal.
  - Also, in several Member States, the exercise of the right of withdrawal from the credit agreement results in a de facto right of withdrawal from the product or service sales contract. Under such circumstances it is easy to understand why a supplier would wait until the end of the 7-day withdrawal period before delivering its product or providing its service. It would be unacceptable for suppliers to have a product that has lost a significant part of its value returned after a few days. Amendment No. 106 put to a vote at the European Parliament's Plenary specifically addressed this issue of credit at the point of sale. EBIC favours this amendment.
  - When the consumer, by express agreement in writing, freely chooses to receive immediately delivery of goods/services financed by credit, this should contextually constitute a waiver to the 7-day right of withdrawal from the credit agreement. A right to a waiver should be offered to allow this, upon clear and understandable warning by the lender that the right of withdrawal is thereby, waived. Alternatively as it is already the case in France for “crédit affecté”, the waiver could be coupled with a period of three days in order to guarantee the consumer a time for reflection.
  - Furthermore, EBIC considers that the exercise of the right of withdrawal should ensure maximum security for all parties involved. The issue of the exact moment at which the withdrawal period begins is quite important to lenders and the solution provided in Article 11-1 is unsatisfactory. The time at which the credit contract is presented to the lender is not a suitable criterion, since it is not sufficiently precise, is subject to different interpretations and therefore disputes. It will oblige lenders, who will be looking for some form of indisputable evidence, to implement time-consuming and costly procedures for monitoring the exact time at which contracts are sent or received. The day the contract is signed would be a more pertinent criterion, since it is undisputedly the time when the customer, informed of the terms and conditions of the credit transaction, expresses his or her consent.

Therefore, EBIC proposes that:

- i) The withdrawal period be reduced to seven days; and
- ii) The consumer be granted the right to ask for immediate delivery of the financed goods/services upon express request in writing, thereby waiving the right of withdrawal.

Alternatively:

- iii) The right to request immediate delivery may be coupled with a three-day reflection period.
- iv) We recommend adoption of the three-day reflection period with a specific regard to credit at the point of sale, to mirror the existing legal framework of some of the Member States.

#### **F. Linked Credit Agreements, Art. 2-pa and Art. 19**

The European Parliament has decided to introduce the concept of linked credit agreement into EU law.

EBIC considers that the definition of linked credit agreement as presented in the new Article 2 – pa voted by the Plenary is excessively broad. The fact that any credit agreement that finances a contract to purchase a product or service could be assumed to be "linked" would cause most credit transactions to be considered linked credit agreements, without the lender, the consumer or the supplier of the product or service having intended to become a party to a "single commercial transaction" (in the original version of the amendment, in German, the criterion of "economic entity or unity" is even broader.) This would be the case for example of a consumer who uses a credit card. Would not every purchase that he or she makes using a card with revolving credit risk being considered a "single commercial transaction"? Would a bank that grants a personal loan to a client that uses the money made available in his or her account to purchase a product or service be assumed to have conducted a linked credit transaction, without the lender possibly even being aware of the purchase?

The consequences of the provisions on linked credit agreements as stipulated in the new Article 19 voted by the European Parliament are too serious for lenders to assume liability without their express and prior consent and what is worse without being informed.

This is why EBIC is asking the European Commission to add an objective legal criterion that clearly connects the lender's liability to the "single commercial transaction" criterion.

Existing legislation in Europe offers two alternative solutions that could be implemented in deference to the subsidiarity principle. Thus, Member States can stipulate that there would be a linked credit agreement either:

- If there is an exclusive relationship between the supplier of the product or service and the lender, or, otherwise.
- If the credit contract expressly identifies the product or the service for the purchase of which it was exclusively granted and the lender pays the supplier directly.

Without such requirements, revolving credit, credit at the point of sale and personal loans that borrowers may repay at their discretion, would be severely compromised.

#### **G. Early repayment of credits, Art. 16**

The European Parliament's legislative resolution stipulates that the consumer shall be entitled to discharge his obligations under a credit agreement at any time before expiry of the period laid down in the agreement and that any indemnity claimed by the creditor for early repayment shall be fair and objective.

These regulations in Article 16 will lead to a considerable increase in credit costs which will be passed on to the consumer and will restrict product diversity and thus the consumer's freedom of choice and decision concerning business transactions.

A right to early repayment of credit agreements should only be allowed under narrowly defined circumstances and if the borrower compensates the bank for all losses which have arisen from the prepayment.

- Paragraph 1

In Art. 16-1, it is not clearly stated, whether this provision shall apply to credits at fixed or variable interest rates. Since credits with variable interest rates are terminable within a short notice period there is no need for a right to early repayment.

There might be such a need in certain cases of fixed interest loans in which the consumer opts specifically for a fixed-rate credit in order to benefit from its inherent advantages or in cases where loans are part of legally determined financial circuit systems as customary inherent in housing policy systems. In return, credit institutions that have to forecast accurately their refinancing, liquidity and cash flow, depend on a consumers' commitment to repay in accordance with the underlying agreement. It would be unfair to burden the banks unilaterally with the risks of a sudden contract-termination by early repayment that jeopardises the rate of interest risk management.

A striking example of the deep impact of the right of early repayment is fixed interest mortgage loans. These credits offering consumers attractive interest rates could no longer be offered in the same way as hitherto. This would be to the detriment to consumers who are interested in a consistent basis for their budgeting calculation and would also deprive them of effective protection against interest rate fluctuations.

- Paragraph 2

The regulation concerning the indemnity in Art. 16-2, especially the notion "fair", is far too vague and should be deleted. The terms may be interpreted in different ways on the national levels or by the judiciary bodies faced with litigations about this issue. Any disparity in interpretations could be counter-productive.

A penalty for early repayment should indemnify the lender for the loss of margin and costs caused by the early repayment. Early repayment completely free of charge would disadvantage consumers who have entered into fixed-term obligations and stick to the period for which their credit agreements run as they would also have to bear the additional costs resulting from early cancellations.

## **H. Credit Intermediaries, Art. 2-d and 2-da**

The term "credit intermediary" should be restricted to any natural or legal person whose principal activity consists in offering and or concluding credit agreements for remuneration. This does not apply to sellers whose main activity is the sale of goods or services other than credit.

Sellers are not credit professionals and this is why they work with credit institutions. Their role is limited to, on the one hand, information provision (the terms of which are defined by the lender) and on the other hand, data transfer the content of which is validated by the lender himself. Sellers and lenders are presently partners and they are mutually dependant on the standard of each other's behaviour. It is in the seller's interest to have a partner who keeps customers satisfied in terms of prices and quality because this helps promoting sales. It is also in the advantage of the lender to have a partner who can transfer data accurately, check documents appropriately and offer good service to the customer. These are necessary prerequisites for adequate credit risk management. Markets being nowadays extremely competitive, the partnership between seller and lender only will last if both parties are satisfied.

Legal provisions subjecting average sellers to the control of a body in charge of credit intermediaries supervision, to the obligations linked to an actual duty to advice or to any upcoming comprehensive regulation, would not improve consumers protection under today's prevailing economic conditions. On the contrary, this would clearly increase the general cost of credit, sellers being forced to comply with obligations deriving from additional bureaucracy. This would even be a deterrent for sellers to cooperate in the credit distribution sector.

While it is reasonable to define rules for professional credit brokers and to supervise them, the same regulation could not be applied to dealers and merchants. This is due to the excessively high number of entities being potentially subject to supervision. No effective supervision can be put in place in these conditions.

### **I. Annual Percentage Rate of Charge (APRC), Art. 12 (Art. 13, according to the original proposal)**

EBIC feels that a single APRC including exclusively those costs levied by the lender for his benefit should be retained in the directive as this is the only way to provide a useful and consistent means of comparison for consumers.

Indeed, the purpose of an APRC is comparability. It enables consumers to compare the products available to them on both national and cross-border basis. The key condition for comparability is that the APRC is calculated in the same way, and therefore includes the same components in all Member States, so that consumers can compare the same piece of information.

In this respect, only the Total Lending Rate (TLR) as defined under former Article 13 of the Commission proposal fulfils this comparability condition and can therefore be of use to consumers. The TLR includes those costs levied by the lender for his benefit, which are similar throughout Member States. EBIC believes that this is the rate that must be named APRC and maintained in the Directive.

As far as the specific costs to be included are concerned, the APRC should be based on those costs levied by the lender for his benefit. The APRC should therefore include:

- Net interest (including credit insurance, if any);
- Administrative costs (file);
- Survey costs (levied by the lender for his benefit), if any.

APRC should exclude, in particular:

- Costs of any insurance taken out by the consumer;
- The costs of establishing the security/guarantee. Costs for creating the security, and notably the notary fee, depend on the location of the pledge; the credit institution does not set or charge them and would normally not be able to know their precise amount before the loan contract is signed.

Further to a specific request by the EU Commission, EBIC would wish to provide an explanation as to why the inclusion of third party registration costs would hamper comparability: In an internet based approach by a consumer, a lender can not necessarily know about the location of the property and would use the registration fee in his own country. Inclusion of these costs is however irrelevant, as a potential borrower has one specific property in mind and does therefore not require to be informed about registration/notary fees from all the different lenders in different Member States. Instead, he requires only the costs which are relevant in the country where his property is located. These costs will be indicated to him in the ESIS, the European Standardised Information Sheet. Moreover, in some national contexts, i.e. in the Netherlands, notary fees are no longer pre-fixed for the national territory. Forcing all lenders to include costs of establishing the security/guarantee can therefore hinder comparability in a cross-border context.

Conversely, the wide APRC as provided in former Art. 12 of the Commission Proposal and including all costs, which consumers face when taking out a loan, should be removed as it does not in any way allow comparison. Indeed, as this wide rate would de facto include a wide range of costs, which vary from one Member State to another, it would result in different pricing examples, and therefore be misleading, should it be used as a means of comparison. In addition, the obligation to disclose the “total cost of credit” as foreseen in Art. 6 does already cover these costs thereby informing the consumer effectively about his future financial burden/obligation. Against this background, the APRC should not be used to illustrate the overall cost of a credit, because consumers expect comparison from an APRC. As it is impossible for a creditor to determine the total amount of the costs a consumer must pay to the creditor and to other parties in relation to the credit agreement, an APRC based on these costs would be incorrect.

Furthermore, EBIC members strongly believe that the method of calculation of the APRC adopted by the Parliament in first reading would equally impede comparability for two reasons:

- The calculation of APRC taking into account “linked transactions” as proposed by the Parliament would lead to mathematically ambiguous results. A credit can be financed via repayment vehicles aiming at accumulating capital from savings, insurance or securities products. In this case the credit is not repaid by the consumer in monthly instalments, rather the consumer accumulates the capital needed to pay back the loan in one of the above mentioned repayment vehicles. As a result, two different processes are linked together: the capital accumulation phase has the character of a yield, while the loan process represents a cost factor to the consumer. Mathematically however, the cash value equations as highlighted in the calculation examples provided in the original Commission text sometimes lead to more than one APRC figure and sometimes no APRC can be calculated at all.

In conclusion, it can be stated that the inclusion of capital accumulation processes in the calculation of APRC leads to mathematically incorrect results. In cases where security products are used as a repayment vehicle, a lender is faced with the additional problem that he cannot know the exact amount of interest accrued from the securities product. At best, the lender could make an estimation of the capital accumulation to be incorporated in the calculation of the APRC, which - in most cases - will lead to an incorrect result. When combining insurance products with a credit, the proposed mathematical combination of the insurance product with the loan in one single APRC would furthermore ignore the fact that the insurance product provides an additional value to the borrower. The insurance as such is an additional service, which cannot be expressed in mathematical terms (examples further illustrating the mathematical problem of combining yield and cost transactions can be provided to the Commission on request).

- A calculation method taking account of the exact days per month would make the APRC dependent on the month the offer is requested. As calendar months consist of different numbers of days, the APRC will change depending on the month the borrower requests an offer, notwithstanding the fact that the nominal rate remains the same. Changing to the daily calculation method would therefore potentially mislead borrowers by indicating a different APRC figure depending on whether he/she has requested the credit offer in January (31 days) or February (28 or 29 days). Lenders wish to inform borrowers (through the APRC) on the cost of their credits based on the quality of the loan regardless of the days of the month in which the loan offer is made. In contrast, the current practice of standardization of the time period used as a reference to calculate the APRC makes sense and should continue to be used. Against this background, EBIC would recommend that the APRC should be calculated by taking account of equal fractions of a year (standardized time reference).

### **ANNEX : Mathematical examples on the daily calculation of an APRC**

In the opinion of the EBIC members, the calculation of the annual percentage rate of charge should in principle be based on only a narrow concept of the effective interest rate which should be confined solely to the cost factors which are generated or can be influenced by the credit institution itself.

Art. 12 (1) adopted by the EP in plenary would in particular result in taking into account; *“the exact day determination for the term of the loan relevant for the calculation (Exponent ..., expressed in days divided by 365.25”* (365.325 is a typing error).

Exact day calculation of the term of the loan for the calculation of the annual percentage rate of charge – in contrast to the usual practice nowadays throughout Europe of equal fractions of a year – would lead to the following problems:

#### **Exact time of calculation with an example**

For further illustration of the mathematical problems arising due to a daily calculation of an APRC, we provide the following calculation example:

A credit sum of € 6.000 will be paid. One month later the repayment period starts with 48 monthly payment of € 149,31, the last payment rate will be paid 4 years after the credit has been paid out.

The time period (in years) will be calculated by the amount of calendar days between beginning and the end of the relevant time frame divided by 365,25. To clearly mark out the effects resulting due to the different lengths of months, the date when the credit is paid off has been changed within a period of 4 years every month. (Therefore it is irrelevant that the first payment was done on the 15<sup>th</sup> of a month: for starting days between the 1<sup>st</sup> and the 28<sup>th</sup> one get identical results.)

This table shows the influence of the date of payment of the credit by the bank on the APRC. Additional to this the smallest and highest value is shown. The last line show the APRC, if the APRC is calculated on a monthly basis such as below.

Date dd.mm.	2002	2003	2004	2005
APRC if credit is paid out on dd.mm.yyyy				
15.01.	9,3924%	9,3888%	9,3848%	9,3957%
15.02.	9,4004%	9,3968%	9,3928%	9,4038%
15.03.	9,3663%	9,3626%	9,3726%	9,3696%
15.04.	9,3740%	9,3704%	9,3805%	9,3774%
15.05.	9,3678%	9,3641%	9,3743%	9,3712%
15.06.	9,3757%	9,3719%	9,3822%	9,3791%
15.07.	9,3695%	9,3657%	9,3761%	9,3729%
15.08.	9,3773%	9,3735%	9,3839%	9,3808%
15.09.	9,3852%	9,3814%	9,3919%	9,3887%
15.10.	9,3791%	9,3752%	9,3858%	9,3826%
15.11.	9,3870%	9,3831%	9,3938%	9,3905%
15.12.	9,3809%	9,3769%	9,3877%	9,3844%
Minimum				9,3626%
Maximum				9,4038%
Average				9,3806%
constant distance: 1 month = 1/12 year				9,3806%

## **ANNEX 2: General principles and methodology for identifying and prioritising further EU level legislative actions and for improving the EU financial rule-making process**

### **Type of regulation: Self-regulation as an alternative to binding regulation**

- Application range: There is a broad range of approaches to self-regulation including:
  - ⇒ codes of conduct: bilateral or multilateral agreements between different parties (typically banks and their customers), e.g. the European Code of Conduct on Home Loans,
  - ⇒ market conventions or market driven standards: agreements amongst industry participants on standards or infrastructural tools, for instance, in the clearing and settlement area (e.g. the Master Agreement for Financial Transactions (EMA) and Euribor, Eonia and Eurepo benchmark rates);
  - ⇒ good practice guidelines: usually undertaken unilaterally by one organisation or a group of organisations;
  - ⇒ industry sponsored accreditation.
- Advantages and disadvantages of self-regulation: To illustrate pros and cons, EBIC would like to focus on codes of conduct in the EU:

#### ⇒ Advantages of codes of conduct:

First, codes of conduct were originally designed to put the initiative in the hands of a non-regulator. They were initiatives by the industry, or even an individual company, to promote good practice and to indicate goodwill to a specific sector/customer group.

Second, self-regulation utilises industry resources and expertise unavailable to government. Industry assumes responsibility for concerns raised by the community and is able to work directly with stakeholders to resolve outstanding issues.

Third, codes of conduct have sometimes been used to avoid the need for legislative action. Codes of conduct offer a novel solution to the sometimes burdensome problem of legislative or regulatory procedures.

Fourth, codes of conduct can be adopted by the parties concerned with a great deal of speed. Self-regulation allows industry the flexibility to offer greater choice for consumers and be more responsive to changing consumer expectations. It is usually more adaptable than binding regulation.

#### ⇒ Disadvantages of codes of conduct:

First, the concept of “code of conduct” is not uniformly understood in the EU, where two different models of self-regulation co-exist:

- The Binding Model (British, Irish and to some extent Dutch models): the concept of self-regulation is well established in some countries. Banks and consumers have a long and positive tradition of working with codes. There is an understanding that a Code is equivalent to binding legislation as the bank has to comply. In general, compliance bodies regularly monitor the correct implementation of the Code. For instance, the UK Code is independently reviewed biennially, involving detailed discussions with all stakeholders (including government, consumer groups, the industry and its regulators). Because the Codes are public documents, other mechanisms are effective in ensuring enforcement, e.g. the press.
- The Non-Binding Model (Continental European tradition): in contrast, in continental Europe, Member States commonly use binding legislation/regulation to govern the banking business. Self-regulation is, so far, understood as being complementary to or rather providing interpretation of binding legislation.

Many of the misunderstandings surrounding the code of conduct concept arise from its precipitate transposition in the EU, and the lack of proper education of the parties concerned.

Second, lies the question of precedent setting judicial interpretation: to date, no judiciary rulings can be found in the EU to support the view that codes of conduct are binding, and to find industry liable. A US court, however, has concluded that a voluntary code was binding. In *Kasky / Nike*, a ruling of 2 May 2002, a California Court treated Nike's public communications regarding its child labour policy as ordinary product advertisement which could establish liability if the content of such communications was found to be false. In the context of the home loan agreement, the Commission services equally argued that the failure of an individual credit institution to implement the home loan agreement - notwithstanding public registration and announcements - could eventually be interpreted as a breach of the directive on misleading advertisement.

Third, European law supersedes national law – but national law supersedes European Codes of Conduct. Many credit institutions struggle with conflicting provisions where implementing the European home loan agreement.

Fourth, at the European level, there is no guarantee that the negotiation and adoption of a code of conduct will be undertaken swiftly (e.g. the EU code of conduct on home loan agreements).

- Pre-requisites for the effectiveness of self-regulation in banking:
  - ⇒ Self-regulation, like binding legislation, should promote further integration and ultimately benefit customers and market participants alike.
  - ⇒ Self-regulation is unlikely to be effective in an area where regulation already exists at Member State level, unless the decision is taken that self-regulation should replace/supersede national regulation.
  - ⇒ Furthermore, there is a need for the European Institutions to clearly define how European codes of conduct or self-regulation in general should be understood and accordingly implemented at the national level.

- ⇒ Legal certainty should be provided as to the conditions under which self-regulation does not breach competition law.
- ⇒ Involvement of the European regulator in self-regulation: Such involvement is justified or even to be recommended in so far as he can assist in facilitating the design of self-regulation and in integrating the scheme into the regulatory framework (the EU Home Loan Code was published via an EU communication).
- ⇒ Comparative costs of self-regulation and binding regulation: Self-regulatory schemes promote good practice at affordable costs, generally perceived to be lower than those implied by binding regulation.
- ⇒ Cost Benefit Analysis for industry: There needs to be perceived benefits for those promoting self-regulation. These benefits can be direct, for instance a boost to their sales, or indirect, such as lesser regulatory capital costs.
- ⇒ Proper and effective administration of the schemes (binding model): For a scheme to be successful there needs to be consumer awareness. Schemes should be transparent to beneficiaries. This can be achieved by making sure that beneficiaries are consulted and that the schemes are also promoted by the partner in a bilaterally negotiated code of conduct (i.e. the representative body of the beneficiary – the EU code of conduct on home loans however suffered from the fact that consumer organisations refrained from promoting the code).
- ⇒ Code administration bodies should regularly review the appropriateness of self-regulatory schemes in consultation with government and consumer groups. Forming a body separate from industry is often perceived as preferable to relying on industry associations as it enables equal representation of all stakeholders and is therefore immune from bias.
- ⇒ Any funding arrangement for self-regulation should be transparent and avoid putting some businesses at a disadvantage.
- ⇒ Complaint handling mechanisms: To be effective at addressing consumer concerns, a code needs to address consumer complaints and set performance standards for participants. Effective dispute resolution schemes are crucial.

### **ANNEX 3: Specific issues identified for further attention by EU policy-makers**

#### ***Company taxation: Elimination of problems related to cross-border losses and transfer pricing***

The lack of ability to set off tax losses in one Member State against taxable profits in another Member State results in excessive tax costs. In the worst case the tax exceeds overall profit. There is an urgent need for legislative changes to allow losses of companies to be set off against taxable profits of related companies resident elsewhere in the EU. Therefore EBIC looks forward to seeing the innovative solution which the Commission announced it would propose.

Double taxation arises where one country makes an adjustment to taxable profits on intra-group transactions and the second country fails to make a corresponding adjustment. EBIC believes that there is a need for an EU-wide accepted form of documentation regarding intra-group transactions and transfer pricing adjustments. In addition, all tax treaties should be updated to OECD standards. Above all, financial institutions need binding arbitration procedures to avoid double taxation.

The issue of capital allocation to branches has not been specifically addressed by the Commission but is of primary concern to EBIC. Unless there is a common EU-wide interpretation of deemed branch capital, double taxation is likely to occur. Capital attributions to branches should be consistent and there should be binding arbitration to ensure that any tax adjustment is matched by an equivalent reciprocal adjustment in profits at Head Office level. EBIC is further concerned that tax discrimination still arises whereby a Member State gives more favourable tax depreciation for assets leased locally compared with assets leased to customers in another Member State. There is a need for an equal relief for capital equipment leased cross-border and capital equipment leased domestically.

#### ***Withholding tax on interest payments made between companies***

Withholding tax on interest payments between companies results in a lack of competition. When a withholding tax is imposed, resident EU banks are put at a disadvantage compared with local banks within a country. There should be no withholding tax on intra-EU cross-border interest payments between companies.

#### ***Legal certainty about VAT treatment of financial services***

The current VAT treatment of financial services causes major problems for the European financial industry. VAT on intra-group cross-border transactions, and in some cases within one country, prevent the efficient organization of business. Due to their reduced right to deduct input VAT, financial institutions incur multiple VAT taxation on intra-group allocations of external costs. Centralized internal costs (payroll costs, self-developed software, Head Office costs) that are allocated to other group entities result in substantial additional costs where there are no VAT grouping provisions. European financial groups would only be able to maintain a competitive position in global financial markets if they are given the opportunity to cooperate, integrate and centralize their functions in a VAT neutral way in order to achieve synergies and structural cost savings.

In addition, the European financial sector has to cope with legal uncertainty about the VAT treatment of financial services.

## **ANNEX 4**

### **Introduction of EBIC**

EBIC is a co-operation of banking associations with a mandate to provide advice, assure a comprehensive consultation of market participants and ensure a representative industry view throughout the process of drafting, adopting, implementing and enforcing EU-financial legislation and thereby provide input for the European institutions and their relevant sectoral committees. It is amongst the declared aims of EBIC to advise the Commission on relevant legislative banking and cross-sectoral initiatives and any developments at Community level affecting the banking and financial services activities associated with the establishment of a European Single Market for financial services.

EBIC has been established by the main banking industry federations: the European Banking Federation (EBF), the European Savings Banks Group (ESBG), the European Association of Cooperative banks (EACB), the European Mortgage Federation (EMF), the European Federation of Building Societies (EFBS), the European Federation of Finance House Associations (Eurofinas) / the European Federation of Leasing Company Associations (Leaseurope), and the European Association of Public Banks (EAPB).