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The Over-indebtedness of European Consumers – a View from Six Countries

Edited by Irina Domurath, Guido Comparato and Hans-W. Micklitz

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European Regulatory Private Law: The Transformation of European Private Law from Autonomy to Functionalism in Competition and Regulation (ERPL)

A 60 month European Research Council grant has been awarded to Prof. Hans-Wolfgang Micklitz for the project "European Regulatory Private Law: the Transformation of European Private Law from Autonomy to Functionalism in Competition and Regulation" (ERPL).
The focus of the socio-legal project lies in the search for a normative model which could shape a self-sufficient European private legal order in its interaction with national private law systems. The project aims at a new–orientation of the structures and methods of European private law based on its transformation from autonomy to functionalism in competition and regulation. It suggests the emergence of a self-sufficient European private law, composed of three different layers (1) the sectorial substance of ERPL, (2) the general principles – provisionally termed competitive contract law – and (3) common principles of civil law. It elaborates on the interaction between ERPL and national private law systems around four normative models: (1) intrusion and substitution, (2) conflict and resistance, (3) hybridisation and (4) convergence. It analyses the new order of values, enshrined in the concept of access justice (Zugangsgerechtigkeit).

The research leading to these results has received funding from the European Research Council under the European Union's Seventh Framework Programme (FP/2007–2013) / ERC Grant Agreement n. [269722].

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Abstract

Six years into the global economic and financial crisis, many European countries have suffered profound economic, political, and social repercussions. Governmental and constitutional crises, high levels of public debt, the adoption of austerity measures, unprecedented levels of unemployment, and the spreading of poverty have marked many European societies. While the EU is in a process of re-examining the whole design of the banking system with far-reaching political and institutional consequences, the impact of the economic crisis on indebted consumers, and specifically those with mortgages, has been much less discussed. The Working Paper presents the result of a research on the effects of the financial and EURO crisis in six European countries within and outside the Eurozone (Greece, Hungary, Iceland, Portugal, Romania, and Spain) having in common that they received international bailout loans under the condition of implementing intrusive austerity measures. In those countries consumers are still facing increasing levels of (over-)indebtedness and struggle with the effects of the crisis, both in financial and social terms. In this light, the studies pay attention to both the social reality and the legal change which is undergoing as triggered by legislative reforms and judicial decisions. The studies also lay open the shortcomings of a EU consumer policy which is largely based on the image of the reasonably circumspect consumer who is supposed to be autonomous, self-reliant, and reasonably well informed. In this regard, the EU suffers from a clear internal market bias that promotes and requires easy access to consumer and mortgage credit, without paying sufficient attention to the possible drawbacks in terms of social exclusion.

Keywords

over-indebtedness, household debt, financial crisis, internal market, Eurozone

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Editors' Introduction

Six years into the global economic and financial crisis many European countries have suffered profound economic, political, and social repercussions. Governmental and constitutional crises, high levels of public debt, the adoption of austerity measures, unprecedented high levels of unemployment, and increasing poverty have affected many European societies. The EU is currently in the process of re-examining the structure and design of the banking system within the internal market, with far-reaching political and institutional consequences.

The focus has long been on the impact of the crisis on states and on the banks. State default, sovereign debt and bailouts have made the headlines. However, the impact of the economic crisis on consumers, as debtors of consumer credit or as mortgage holders, has raised much less concern. The results presented of this study undertaken between 2013 and 2014 are intended to change the focus and to broaden the debate. The Working Paper presents the results of research which aimed to collect information on the effects of the financial and monetary crisis in six European countries that have been significantly hit by the financial crisis. More specifically, the Working Paper examines the effects of the crisis on indebted consumers with some form of consumer credit or mortgage. In the broader context of the study, the financial crisis of 2008-2009 is the critical time period, while with regards to the law, the Aziz case of the Court of Justice of the European Union (CJEU) is considered a turning point for (over-)indebted consumers.[1]

Each of the countries chosen for the case studies (euro countries: Greece, Portugal, Spain, and non-Euro countries: Hungary, Iceland, and Romania) have in common the fact that they received bailout loans from the Eurozone countries and the IMF under the condition of implementing intrusive austerity measures. While the loans were mainly used to improve the financial position of the banks or the economy in general, austerity measures have affected many social issues. As such, it is necessary to examine the situation of those most affected – namely indebted people with some form of consumer debt or a mortgage on residential property– assessing the effects of a wide range of factors such as the bursting of the housing bubble, the decline in house prices and wages, rising unemployment, and currency depreciation. Such factors will be examined in considering their effect on financial and social inclusion and the danger of exclusion of vulnerable consumers.

In the three non-Euro countries some specific issues have perhaps aggravated the problems consumers face. For instance, Iceland (participating in the EU internal market framework through the EEA Agreement) was the first country to experience the resignation of a government and new elections in 2009. Similarly, in 2012 Hungary and Romania went through constitutional crises. In these countries the vast majority of the loans to private households were connected to foreign currencies with the benefits of lower interest rates and longer maturities but the risk of depreciation of the local currency and subsequent inability of the borrower to repay their foreign currency loans.[2]

All these events have had a direct impact on contract relations and have brought to the fore the importance of the law, most notably private law and private law litigation, before the European courts. This is reflected in important cases that have reached the highest courts in both the Euro- and non-Euro countries as well as the CJEU. Most notably the *Aziz* case has had an immense impact both on Spanish procedural law and on the legal orders of other European States with regards to the interpretation of unfair contractual terms in mortgage agreements. This case not only triggered a

1 Mohamed Aziz v. Caixa d'Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa), C-145/11 (14/3/2013).

2 We have to distinguish between foreign-currency loans (loans denominated in foreign currencies), FX-indexed loans (loans indexed to foreign currencies and thus dependent on the exchange rate), and CPI-indexed loans (loans indexed to the consumer price index thus dependent on inflation). See further on the issue Yesin "Foreign currency loans and systemic risk in Europe", Federal Reserve Bank of St. Louis Review, May/June 2013, 95(3), pp. 219-35. available at http://research.stlouisfed.org/publications/review/13/03/219-236Yesin.pdf.

number of follow-up requests for preliminary rulings from Spanish courts to clarify certain issues but also triggered such requests from other countries (albeit after initial reluctance). For example, the Hungarian Supreme Court requested an important preliminary ruling from the CJEU on questions relating to unilateral changes to loan contracts by banks as well as exchange rate margins.[3] The Icelandic Supreme Court has declared illegal FX-indexed loans and sought an advisory opinion from the EFTA-Court on the legality of CPI-indexed mortgage loans. At the same time, some have criticised the reluctance of national courts to invoke EU law and the consequential lack of protection for consumers. All this factors indicate that private law is considered to be of utmost importance as a means of last resort for solving over-indebtedness issues resulting from mortgage agreements.

The case studies demonstrate that, despite initial signs of cautious macro-economic recovery in 2013,[4] recovery at the micro-economic level remains tentative. This is especially so for consumers with mortgages who are still facing increasing levels of (over-)indebtedness and are struggling with the effects of the crisis, both in financial and social terms. At the same time public policy makers, involved in the bail out of their national banks, have neglected the (at times) dramatic effects of social exclusion. The case studies have also highlighted the shortcomings of EU consumer policy which is largely based on the image of the reasonably circumspect consumer who is autonomous, self-reliant, and reasonably well informed. According to this model, the circumspect consumer is to be empowered, predominantly through the provision of information and competition in the internal market and the asymmetry of information is to be addressed by credit registries and credit bureaus.[5] In this regard, the EU suffers from a clear internal market bias that promotes and requires easy access to consumer and mortgage credit. Such policy is very much in line with the Anglo-American vision of "cheap money" as a means of achieving financial and social inclusion. The 2008 crisis however provoked quite the opposite, namely over-indebtedness in turn yielding financial and social exclusion without a European policy to counteract such effects.

In the post-crisis context new regulatory mechanisms and private law rules are currently being designed at the supranational and national level in order to tackle such issues. Knowledge of the concrete issues, problems, and tentative solutions tested in the relevant countries analysed in this study is crucial in order to have an informed opinion on these issues.

The study was designed as a cross-country study. The information collection could be used for a comparative analysis of the different legal frameworks in the six countries – including legislation and jurisprudence – against a factual background deriving from empirical data relating to over-indebtedness. To this end the rapporteurs for each country were required to answer a broad questionnaire with the help of many different sources: statistics and empirical sources, legal sources, policy documents, and secondary academic sources amongst others. Whenever data collection proved insufficient the rapporteurs were encouraged to collect primary data themselves through interviews with affected parties. To this end, most rapporteurs conducted semi-structured interviews with different parties such as consumers, bank employees, or representatives from consumer organisations.

Given the broad design of the questionnaire and its aim of providing information on the larger context of over-indebtedness, the cross-country study naturally has limitations with regard to the in-depth

3 Árpád Kásler, Hajnalka Káslerné Rábai v. OTP Jelzálogbank Zrt, C-26/13, Judgment of 30 April 2014.

4 Recent developments since 2013 have been cautiously interpreted as first signs of economic recovery have been identified on both sides of the Atlantic, see for example in the U.S. http://www.economist.com/node/21550256, Portugal http://www.economist.com/news/europe/21584346-few-crumbs-cheer-count-welcome-good-news-between-bail-outs, Spain

http://www.ft.com/cms/s/0/4a56f51c-2b60-11e3-bfe2-00144feab7de.html#axzz2suJHGJzv, http://www.economist.com/news/europe/21587811-mariano-rajoy-predicts-economic-joy-spain-still-has-long-way-go-worst-may-be-over, and Greece http://www.economist.com/news/finance-and-economics/21577076-back-source-euro-zone-crisis-daring-hope-fearing-fail.

5 See in this regard OECD Discussion Paper on Information Sharing "Facilitating Access to Finance", available at http://www.oecd.org/investment/psd/45370071.pdf.

collection of data. Moreover, comprehensive data collection proved difficult at times. For instance, consistent parameters for the measurement of concepts such as over-indebtedness do not always exist, either at the domestic or the European level. Moreover, data collection within one country often turned out to be incomplete. Finally, given the social sensitivity of the topic and its connection to sensitive business information, gaps in data could not always be filled through interviews.

This research and the conference entitled "The over-indebtedness of European consumers after the financial crisis" at the European University Institute in November 2013, where the preliminary results of the studies were presented, would not have been possible without external funding. We would like to thank Schufa Credit bureau in Germany. The overall activities form part of the ERC Grant of Professor Micklitz on 'European Regulatory Private Law'. The conference provided a formidable forum for discussion. It brought together academics with representatives from the European Commission, providers of financial services, credit bureaus, and consumer organisations. Comments and feedback are integrated in the reports. We would like to thank the participants for their commitment and their preparedness to engage in a largely unknown territory.

CASE STUDIES: EURO COUNTRIES

GREECE

Georgios Mentis and Katerina Pantazatou[1]

Preliminary Information

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

Although Law 3869/2010 is devoted to over-indebted natural persons it does not directly provide for a definition of the term. Under Article 1, however, the term is implicitly defined[2], as 'the permanent inability of natural persons[3] to pay their overdue financial debts, as long as this is inability is not based on fraudulent behaviour'. In other words, over-indebtedness is considered a situation in which the debt payment owed by the consumer exceeds his financial capacity.[4]

If the inability to repay is based on fraudulent or intentional behaviour the bankruptcy court will reject the debtor's application to be covered by Law 3869/2010. Intention, in this sense, is understood as the intentional failure to repay the debt, despite the existence of liquidity by the debtor, for instance by channelling existing capital to banks outside the country so that they become inaccessible to the creditor. The burden of proof with regards to intention lies with the creditor. The intention of the debtor as an element that excludes the debtor from the scope of Law 3869/2010 is an issue addressed by the Court during the hearing of the application. Furthermore, Art. 1 (2)β of Law 3869/2010 provides that claims that arose from intentional delict/tort are not covered by the Law at issue. Similarly, claims arising from post-dated or "bounced' cheques are not exempted from the application of Law 3869/2010.[5]

It is worth mentioning that in the Explanatory Statement of Law 3869/2010 the concept of over-indebtedness is underlined as the main social problem in Greece, caused by various factors such as the financial crisis, the high interest rates applicable to consumer credit, the aggressive lending practices, the bad (financial) planning from the consumer's part, unforeseeable occurrences such as lay-offs and the overall lack of a consumer-supportive institutional framework.

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1 We would like to thank Mr. Viktor Tsiafoutis, Attorney at Law, Athens and Mrs. Olga Aloupi, Attorney at Law-LLM Candidate, for their substantial assistance in the preparation of this report.

2 Free translation.

3 And thus not of persons who have the ability to go bankrupt – merchants, for instance are covered by the 'Insolvency/Bankruptcy Code'.

4 See Mentis G. Defence and Release of the over-indebted debtor, Dikaio kai Oikonomia P.N. Sakkoulas (2012), p. 1. [in Greek: Μεντής Γ., Άμυνα και Ελευθέρωση του Υπερχρεωμένου Οφειλέτη: Η πορεία προς μια νέα σεισάχθεια στα όρια μεταξύ αστικού δικαίου και νέου πτωχευτικού δικαίου, Δίκαιο και Οικονομία Π. Ν. Σάκκουλας (2012), σελ. 1.

5 See Roussos, Over-indebted natural persons, Applications of Civil Law 2010, 1297 et seq. [in Greek: Ρούσσος Κ., Υπερχρεωμένα Φυσικά Πρόσωπα, ΕφΑΔ 2010, 1287 επ.]

2. Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?

The concept of the vulnerable consumer is not defined in the national legal order with regard to the 'consumption' of financial services. In contrast, the term is defined in Art. 52 of Law 4001/2011[6] where it is stated that the 'vulnerable costumer' (as defined therein as persons of low income, families with more than three children, long-term unemployed persons, persons with disabilities, persons living in remote areas and persons that require mechanical/artificial support) is to benefit from lower tariffs and more favourable regulation in the consumption of electricity.

3. Is the term "poverty" or "low-income consumer" defined in the national legal order?

Neither the term 'poverty' nor the term 'low-income consumer' is defined in the national legal order. In contrast, in several laws or ministerial decisions a definition of 'low income citizen' or low-income 'groups' and 'persons' is provided.[7] The Hellenic Statistical Authority (EL.STAT) in its Statistics on Income and Living Conditions for 2012[8] defines poverty through reference to the OECD definition, using the modified OECD equivalence scale.
In Law 3869/2010 on the regulation of debts of over-indebted individuals-non merchants (households) (article 8 par. 5) it is provided that in exceptional circumstances, such as unemployment, health problems and cases of *insufficient income to meet basic living needs* the court may determine that the debtor will pay "zero instalments" (Nullplan) to his creditors, meaning that the debt should be discharged altogether.

II. Numbers on over-indebtedness

1. How many consumers are considered "indebted" in the country? (since 2000)

To date household debt amounts to approximately €75 billion for mortgages and €35 billion for consumer credit and credit cards. EKPOIZO's data (more than 12,000 files which have not yet been digitalised) provide that on average every household with a mortgage has a debt of €120,000-150,000. There are also households that only have consumer credit. This data in conjunction with the fact that approximately 1.5 million mortgage or housing loans have been given, allow us to estimate the number of consumers who are indebted as being approximately two million *(*estimation according to the Bulletin of Conjunctural [sic] Indicators', Bank of Greece, November-December 2013*)*

6 See also the Decisions of the Ministry of Environment, Energy and Climate Change Δ5-ΗΛ/Β/Φ29/16027/6.8.10 as amended by the Ministerial Decisions Δ5-ΗΛ/Β/Φ29/6713/24.3.11, Δ5-ΗΛ/Β/Φ1.20/οικ.878/17.1.13, Δ5/ΗΛ/Β/Φ29/οικ.21235/20.11.13 and Δ5/ΗΛ/Β/Φ29/οικ.23823/23.12.2013 .

7 See for example Law 3226/2004 (ΦΕΚ 24 Α/4-2-2004) on the provision of legal assistance to 'citizens of low income'. The term is defined under Art. 1 par. 2 which reads: ' Citizens of low income who are eligible for the legal assistance, are those whose family income does not exceed the two thirds of the lowest yearly individual remuneration, as provided in the National General Collective Labour Agreement.'

8http://www.statistics.gr/portal/page/portal/ESYE/BUCKET/A0802/PressReleases/A0802_SFA10_DT_AN_00_2012_08_F_EN.pdf

Table 1 - Total number of Loans (in millions of euros – divided by loan recipients) 2007-2013[1]

Year	Total number of loans	Private loans	Business Loans	Freelancers, Farmers, Personal Businesses
2007	215,405	104,116	111,289	-
2008	249,611	117,203	132,458	-
2009	249,677	119,635	130,043	-
2010	257,846	118,120	123,244	16,483
2011	248,535	113,050	120,126	15,359
2012	227,655	106,530	107,335	13,790
2013*	220,993	119,644	101,349	

*Until November 2013

Table 2 - Loans given to households (divided by loan type, in millions of euros), 2007- November 2013[2]

Year	Total Number of Loans	Change In %	Mortgage/ Housing Loans	Change in %	Consumer Credit	Change in %	Other loans	Change in %
2007	104,116	22.2	69,363	21.5	31,942	22.4%	2,811	35.6
2008	117,203	12.60	77,700	11.2	36,435	16%	3,068	9.5
2009	119,635	3	80,559	3.7	36,044	-1.8%	3,032	-1.1
2010	118,120	- 1.2	80,507	-0.3	35,081	-4.2%	2,532	10.7
2011	113,050	-3.9	78,393	-2.9	32,985	-6.4%	1,672	-2.2
2012	106,530	-3.8	74,634	-3.4	30,236	-5.1%	1,660	3
2013	101,349	-3.5	71,493	-3.2	28,441	-4.5%	1,415	2.5

1 Source: Bank of Greece, 'Bulletin of Conjunctural Indicators', Issue 153 November-December 2013 (Τράπεζα της Ελλάδος, «Στατιστικό Δελτίο Οικονομικής Συγκυρίας», Τεύχος 153 Νοέμβριος-Δεκέμβριος 2013)

2 Source: Bank of Greece, 'Bulletin of Conjunctural Indicators', Issue 153 November-December 2013 (Τράπεζα της Ελλάδος, «Στατιστικό Δελτίο Οικονομικής Συγκυρίας», Τεύχος 153 Νοέμβριος-Δεκέμβριος 2013)

Table 3 – By way of comparison see the same statistics for Germany below:

Year	Total amount of loans	Loans to enterprises	Loans to households			
			Total amount	Housing loans	Consumer Credit	Other
2000	59.330,0	42.360,3	16.969,7	11.271,8	5.511,4	186,5
2001	74.027,4	50.198,7	23.828,7	15.652,2	7.852,0	324,5
2002	86.510,5	55.012,2	31.498,3	21.224,7	9.755,4	518,2
2003	101.178,10	60.979,3	40.198,8	26.534,2	12.409,6	1.255,0
2004	123.993,8	71.433,0	52.560,8	34.052,2	17.053,8	1.454,8
2005	149.903,2	81.009,5	68.893,7	45.419,8	21.825,10	1648,8
2006	179.452,3	93.575,8	85.876,5	57.145,0	26.596,6	2.134,9
2007	215.405,2	111.288,8	104.116,4	69.363,3	31.942,40	2.810,7
2008	225.052,9	107.849,8	117.203,0	77.700,0	36.435,0	3.068,0
2009	249.677,0	130.043,0	119.635,0	80.559,0	36.044,0	3.032,0
2010	257.846	123.244	118.119	80.507	35.081	2.532
2011	248.535	135.485	113.050	78.393	32.985	1.672
2012	227.655	121.125	106.530	74.634	30.236	1.660

In millions of euros

Source: Monthly Report of Deutsche Bundesbank.

Note: From the above comparison we can clearly see one of the factors of the Greek over-indebtedness. In the period from 2000-2009 Greek loans increased 320% while German loans show an increase of only 7.8%. Especially in relation to the household loans, the increase in Greek loans is enormous (almost 600%) while the increase in German loans is around 12%. It is worth mentioning that the income of Greek households is on average almost 40% of the equivalent German income.

a. How many consumers have mortgage debt?

Almost all consumers' mortgage debts are housing loans. Other consumer credits (e.g. credit cards, simple consumer loans) are not usually covered by a mortgage. Approximately 700,000 consumers have mortgage debt.[3]

b. How many consumers have motor vehicle debt?

The system of credit relating to motor vehicles involves not only banks but also specific credit institutions such as credit organizations of the car industries, car rental companies (leasing etc.), credit facilities of car dealers for example. Common statistics for these entities are not available. According to an estimation based on the total number of cars and motorcycles (5,167,557 and 1,556,435 respectively), approximately the one fifth of them (1,000,000 cars and 300,000 motorcycles) is acquired by credit which is still outstanding.

c. How many consumers have other debt (credit card, general consumption)?

Approximately 1,500,000 Greek consumers have other consumer debts.[4]

d. What percentage of those "indebted" consumers / households (a, b, c) is:

i. Single / married

Approximately 20% are single and 80% are married.

ii. With / without children?

3 Estimation according to the Bulletin of Conjunctural Indicators', Bank of Greece, November-December 2013.

4 Estimation according to the Bulletin of Conjunctural Indicators', Bank of Greece, November-December 2013.

Approximately 90% with children and 10% without children.

iii. With / without work?

Approximately 70% with work and 30% without work.

iv. Retired?

Approximately 30% are retired.

v. Low-income consumers?

The answer depends on what it is considered as "low-income". However, more than 50% of indebted consumers have to be considered for the time being as "low-income" consumers.

2. How many consumers are considered "over-indebted" in the country? (since 2000)

Since there is no reliable way to count the 'over-indebted' consumers in the country, we take as an indicator of the 'over-indebtedness' of consumers, delay in the repayment of loan instalments (or the unilateral contract termination by the consumer). Indicatively, in 2007 the total number of loans that were not repaid on time amounted to 4.5% while in 2011 this had reached 14.7% (an increase of 30.6%). According to data from the Bank of Greece in December 2012 approximately 24.5% (an increase of 8.5%)of the housing loans were not paid ('red loans'). This percentage for consumer credit amounts to approximately 38.8%. In June 2013, payments were in arrears in 29.3% of loans while in March 2014 it is estimated (from data provided by EKPOIZO) that 35% of consumers are behind with the repayment of loan instalments. At the same time, at least 65,000 applications have been filed by consumers seeking to benefit from Law 3869/2010 (for over-indebted households), and the number of applications has continued to rise. This data allows us to conclude that approximately 700,000 households could be considered as being over-indebted.

Table 4 is demonstrative of the delays in loan repayments:

Table 4 - Delays in loans repayments (in millions Euros) 2007-2013[5]

Year	Total Number of Loans	Mortgages	Consumer credit	Business Loans
2007	4.5%	3.6%	6%	4.6%
2008	5%	5.3%	8.2%	4.3%
2009	7.7%	7.4%	13.4%	6.7%
2010	10.4%	10%	20.5%	8.7%
2011	16%	14.9%	28.8%	14.2%
2012	24.5%	21.4%	38.8%	23.4%
2013*	29.3%	24%	43.8%	29.2%

* June 2013

According to the Annual Report of Economic and Social Statistics of another statistic company (VPRC)[6] in 2009, a total of 41% of the Greek population was indebted to banks. This figure includes mortgage loans, consumer loans and credit cards. Furthermore, 63% of the public sector employees are indebted with loans and credit cards, while the figure for private sector employees is 51 %.

5 Source: Bank of Greece, 'Bulletin of Conjunctural Indicators', Issue 145 July – August 2012 and Bank of Greece, "Monetary Policy", 2012-2013.

6 VPRC is one of the biggest private companies in Greece for social and political research, and is a member of ESOMAR (European Society for Opinion) and Marketing Research and WAPOR (World Association for Public Opinion Research).

According to the same source, in 2009 77% of indebted consumers faced difficulties in paying off their debt. In comparison with the total population of Greece over 32% of the Greeks faced difficulties in paying off their loan debt.

a. How many individual consumers / households are behind with the repayment of (up to 3 months and more than 3 months):[7]

In Greece, there is no specific statistic differentiation between delay in payment up to three months and more than three months. As of March 2014, on average payment is in arrears in 35% of consumer loans (up from 29% in June 2013 according to the Central Bank of Greece). This means that more than 700,000 households are now behind with the repayment of their credit obligations.

i. General consumption loans

Approximately 750,000 consumers are behind with the repayment of general consumption loans.

ii. Motor vehicle loans

Approximately 500,000 consumers with cars and 150,000 with motorcycles are behind with the payment of instalments.

iii. Student loans

No data available. Independently of this, student loans are very rare in the Greek credit market.

iv. Credit card debt

Approximately 750,000 consumers are behind with the repayment of credit card debt.

v. Mortgages / housing loans

Approximately 200,000 consumers are behind with the repayment of mortgage loans.

vi. Interests

No special data available. Approximately all indebted consumers (2,000,000) owe default interest because of the delay in repayment.

b. How many individual consumers / households have initiated bankruptcy proceedings?

Although 'bankruptcy proceedings' in the strict sense of the term are not available for individual consumers (these are reserved for traders); according to Article 4 of Law 3869/2010 consumers can lodge a petition with the local Magistrate Court to settle their debts.[8] By reference to this procedure, the first official available data from the Magistrate Court of Athens[9] indicates that the total number of applications for debt settlement provided in Article 4 paragraph 1 of Law 3869/2010 that have been submitted from 1 September 2009 to 6 September 2012 in the Magistrate Courts of Greece is 26,869, out of which 6,641 has been submitted to the Magistrate Court of Athens. Data from the General Secretariat for Consumer Affairs (Γενική Γραμματεία Καταναλωτή) provides that of the 5,000 cases that had been discussed before Courts before the end of September 2012, 3,000 decisions have been issued and published. It is noteworthy that the number of positive (granting debt settlement) and negative (not granting debt settlement)[10] decisions is exactly the same. According to unofficial information from the courts the number of applications has increased rapidly as approximately

7 According to the data provided by EKPOIZO.

8 For the procedure see Section VI, Question 1 a and b

9 Data from the Magistrate Court of Athens. See also

http://www.imerisia.gr/article.asp?catid=26516&subid=2&pubid=112935925

10 Approximately 80% of the negative decisions are attributed to issues with admissibility and only 20% to substantive reasons.

100,000 petitions are now pending in all Magistrate Courts, while in June 2013 only 44,262 applications had been filed. Approximately 5,000 decisions have been issued to date.[11]

c. How high is the average amount of outstanding debt?

Approximately €101,349.000.000 (according to data provided by the Central Bank of Greece).

d. What percentage of those "over-indebted" consumers / households (a and b) is:[12]

i. Single / married

13% of consumers are single, 67% are married, 18% are divorced, and 2% are widowed.

ii. With / without children?

90% have children and 10% are without children.

iii. With / without work?

65% are in work and 35% are without work.

iv. Retired?

17% of over-indebted consumers are retired.

v. Low-income consumers?

The answer depends on what it is considered as "low- income". However, more than 80% of the over-indebted consumers have to be considered for the time being as "low-income" consumers.

III. Numbers on evictions

1. How many evictions have there been per year since 2000 (or later if earlier data not available)?

Approximately, 5.000 evictions have taken place every year since 2000.[13]

The newspaper 'Ethnos' reports that within the first two months of 2011 applications for initiating evictions amounted to approximately 4,000, whereas for the entire year 2010 this number was 8,500.[14]

Data from the Magistrate Court of Athens provides that up to the end of July 2011, the relevant Court had adjudicated 1,315 cases regarding eviction, while in 2010 the total number of applications amounted to 1,736. In other words, during 2011 the average number of eviction cases or applications brought before the Magistrate Court of Athens (competent for tenancy disputes for monthly rent less than €450) amounted to 188 applications per month. The number of actual evictions granted by the District Court of Athens has increased by 17% between 2010 and 2011. The number of evictions that have been executed following the Court's decision, remained at the same level for 2010 and 2011.

While the First Instance Court of Athens adjudicates only tenancy disputes when the immovable property is in Athens (and the monthly rent exceeds €450),[15] we believe that the following table

11 Since June 2011 when the Law was first applied, see under section VI, question 1a, iii

12According to the statistics of the Association of Greek Employed Consumers (October 2013) (http://www.gsee.gr/userfiles/file/2013_BOXES/2013_10_17_%20eeke_statistika.pdf)

13 Data provided by the First Instance Court of Athens.

14 http://www.ethnos.gr/article.asp?catid=22768&subid=2&pubid=55606978

15 The Court of First Instance of Athens [Protodikeio Athinon] is competent to adjudicate cases where the monthly rent exceeds Euro 450, according to Article 662 A – 662 H of the Code of Civil Procedure. For monthly rents below this amount it is the Eirinodikeio (district Court) of each area that is competent to adjudicate tenacy disputes, from which however, we do not have any data.

presents a representative sample of tenancy disputes in Greece, in particular since a large part of the Greek population resides in Athens.

Table of Statistics of applications that were filed to the Protodikeio Athinon (First Instance Court of Athens) under the tenancy disputes procedures between 2005 and February 2011, divided according to procedure.

Table 5

YEAR	Expulsion of tenants[16] [αποβολή από το μίσθιο]	Evictions of tenants [απόδοση μισθίου]	Evictions because of owner occupancy [17]	Utilities /Dispute	Rent (€)
2005	19	3,035		1,413	3,376
2006	5	2,883		1,706	3,514
2007	27	2,369		1,603	3,545
2008	7	2,917		1,753	3,108
2009	5	3,254		1,626	3,744
2010	5	2,632	1	1,399	4,241
2011 until 1/2/2011		216		1,94	498

The rights of the lessor in case the tenant delays payment of the rent are provided in Article 597 of the Greek Civil Code, Articles 662 and 662A of the Greek Code of Civil Procedure, or Article 66 of the Introductory Law CCP (Εισ.ΝΚ.ΠολΔ). Articles 15 and 19 of Law 4055/12, as incorporated in the new Code of Civil Procedure, aim to protect lessors against tenants who consistently fail to meet their obligations. As such, these Articles provide that tenants can be expelled from the property without the need for a formal hearing.

2. *How many evictions took place because of:*

   a. *Unpaid mortgage instalments?*

Approximately 5% of the above total number of evictions took place because of unpaid mortgage instalments. In the last five years the reason for this low percentage is that according to specific legislation (Law 4224/2013) the suspension of the enforcement proceedings is contingent upon on stricter conditions.[18]

   b. *Unpaid monthly rent?*

Approximately 95% of the above total number of evictions took place because of unpaid monthly rent.[19]

3. *Who are the persons affected (percentage of young people, families, retirees, unemployed, level of education, low-income consumers)?*

16 Article 662A of the Code of Civil Procedure provides that: ' […] in case the payment of the rent is delayed because of the tenant's peevishness, […] the lessor can demand the issuance of an order for the return of the usage of the property. The repayment of the rent by the tenant within a month from the default notice excludes the issuance of the relevant order' [free translation without the procedural conditions listed therein]

17 Repealed.

18 Data from Protodikeio Athinon.

19 *Ibid.*

While no comprehensive data is available, data from POMEK illustrates that from the total number of consumers that have sought assistance from POMEK members, approximately 35% are unemployed (the percentage does not take into account self-employed who are out of work). It is worth noting that according to a survey conducted by the NGO KLIMAKA entitled 'Homelessness in Greece-2012: An in-depth research on homelessness in the financial crisis'[20] the vast majority of homeless people are men aged 26 – 55, with one out of five having high or higher education. With regard to 'reasons for their homelessness' almost 30% of the sample listed financial reasons, approximately 17 % listed unemployment and approximately 17% noted insufficient financial support from their families as the main reason for their situation.

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

1. Is the CCD 2008/48 implemented into national law?

The CCD 2008/48 on credit agreements for consumers was transposed into national law on 23 June 2010 by the Common Ministerial Decision (CMD) Z1-699/2010.[21] The CMD Z1-699/2010 repealed the earlier CMD Φ1-983/1991 which had implemented 87/102/EEC for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit.

2. Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?

The CMD Z1-699/2010 implementing Article 1 paragraph 2(a) of the CCD 2008/48 expressly excludes mortgage loans from its scope of application. Article 2 of the CMD Z1-699/2010 states that "from the scope of application of this Decision are excluded: a) credit agreements which are secured with security on immovable property…".

In Article 8, concerning the obligation to assess the creditworthiness of the consumer, the CMD Z1-699/2010 goes beyond the Directive[22] and regulates the legal consequences of the breach of this obligation. Specifically, Paragraph 3 of Article 8 of the CMD states that: "if the creditor breaches through his fault his obligations according to paragraphs 1 and 2 (obligations to assess the creditworthiness of the consumer) of this article, the consumer is discharged from the total cost of the credit, including interests; and he has the obligation to pay only the amount of the capital according to the contracted instalments''. Furthermore, even though it is not expressly mentioned in the article, a further condition is required for the discharge of the consumer debt: the real inability of the consumer to repay this debt.[23]

It is the first time that the national law has provided the discharge of debt due to the inability of the debtor to repay their debt. The main requirement for the application of Paragraph 3 of Article 8 is the fault of the creditor, including fraud or negligence, gross or otherwise. The legal consequence is the

20 http://www.klimaka.org.gr/newsite/KoinApok/Astegoi/Astegoi1.htm

21 Official Government Gazette (ΦΕΚ) B917 20100623.

22 But not beyond the relevant regulation of Belgian law, which in case of fraud or gross negligence of the creditor provides by way of penalty the loss of the capital; Articles 15 and 92 of Belgian Consumer Credit Act article as amended by the act of 13th July 2010,

23 Inability means that the debtor cannot respond to the irresponsibly given credit, keeping at the same time for himself and the persons, that he is obliged to care of, a minimum standard of living, See Mentis G. Defence and Release of the over-indebted debtor, Dikaio kai Oikonomia P.N. Sakkoulas (2012), p. 1. [in Greek: Μεντής Γ., Άμυνα και Ελευθέρωση του Υπερχρεωμένου Οφειλέτη: Η πορεία προς μια νέα σεισάχθεια στα όρια μεταξύ αστικού δικαίου και νέου πτωχευτικού δικαίου, Δίκαιο και Οικονομία Π. Ν. Σάκκουλας (2012), p. 35.

discharge of the total amount of the consumer's debt including interest, default interest, litigation interest, judicial costs, and fees. The consumer has to return the capital in accordance with the instalments agreed in the contract. The loan is converted to being interest free and the creditor loses their fee for providing the credit, showing the punitive character of the provision.

3. With regard to the Mortgage Credit Directive: will there have to be an adjustment of national law? What would be the changes in particular?

The Directive 2008/48, already implemented in Greek law (CMD Z1-699/2010), expressly excludes mortgage credit from its scope of application. As a result, Greek legislation shall be brought into line with the Mortgage Credit Directive by introducing new provisions in relation to the following points (indicatively):

- Legal rules about the minimum content of mortgage credit advertisements (articles 10-11 of the Directive). The existing legal framework on unfair and deceptive advertising (articles 9-9θ of Greek Law 2251/1994 on unfair commercial practices, Article 5 of the Directive 2005/29 on unfair business-to-consumer commercial practices in the internal market) is not sufficient, due to the fact that it simply prohibits certain practices rather than setting out imperative rules.
- Legal rules on minimum pre-contractual information (Articles 14, 15 and 16 of the Directive) or relating to information to be provided during the operation of the contract (Article 13 of the Directive). Despite the fact that the bank's obligation to inform its client based on the principle of good faith (Article 288 of Greek Civil Code) is generally accepted,[24] the specialised information required by article 14 of the Directive cannot be easily drawn from the general provision of Article 288 of the Greek Civil Code.
- Legal rules concerning credit assessments (Article 18 of the Directive) and particularly the creditor's obligation not to give credit where there is any suggestion that the consumer is not creditworthy. This is due to the fact that disputes have already arisen in relation to this point, as some authors argue that in the light of the Article 8 of the Directive 2008/48, such obligation does not exist.[25]
- Legal rules on early repayment (Article 25 of the Directive).
- The provisions of national law which are to transpose the Directive on Mortgage Credit are considered *jus cogens* (i.e. they cannot be set aside by contractual terms in the loan agreements).
- Finally, Law 3419/2005 concerning the General Commercial Registry (Γ.Ε.ΜΗ.) should be adjusted in order to include information that must be recorded in the Registry regarding : 1) all natural persons who directly work with clients in an undertaking that pursues the activity of credit intermediation, 2) the Member State(s) where the intermediary intends to conduct business under the rules on the freedom of establishment or on the freedom to provide services and has informed the competent authority of its home Member State in line with Article 20 of the Proposal ("Registration of credit intermediaries").

4. How is the national legal framework with regard to the UCT 93/13?

Law 2251/1994 transposed Dir. 93/13/EEC into Greek law and constitutes the main legal framework for the consumers' protection. Article 2 of the given Law provides an indicative list of unfair contract terms, whereas Article 2 Paragraph 7 provides a non-exhaustive list of specific contract terms that are

24 G. Georgiadis The bank's obligations to inform, enlighten and consult its client (in Greek: Οι υποχρεώσεις της τράπεζας για ενημέρωση, διαφώτιση και παροχή συμβουλών στον πελάτη) ΧρΙΔ 2008, p.865.

25 See Perakis, The principle of responsible lending (in Greek: Η αρχή του υπεύθυνου δανεισμού) ΧρηΔικ 2009, p. 352, Mentis, Defence and Release of the over-indebted debtor, [in Greek: Μεντής Γ., Άμυνα και Ελευθέρωση του Υπερχρεωμένου Οφειλέτη: Η πορεία προς μια νέα σεισάχθεια στα όρια μεταξύ αστικού δικαίου και νέου πτωχευτικού δικαίου) Dikaio kai Oikonomia P.N. Sakkoulas (2012), number 21, Livada, The new European regulatory frame on the consumer credit (in Greek Το νέο ευρωπαϊκό ρυθμιστικό πλαίσιο για την καταναλωτική πίστη) Athens 2008, p. 325.

deemed *ex lege* unfair, and as such void and forbidden. The rules regarding the unfairness of contract terms set out in a specific manner the more general rule that exists in Article 281 of the Greek civil code according to which any abusive or unfair exercise of a right or an institution (in this case, contractual freedom) should be forbidden.[26]

V. Enforcement of consumer credit contracts

1. What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?

Most loan contracts provide that the creditor has the right to terminate the loan agreement in case of the debtor's default on two or three instalments. In market practice, the creditor sends a warning letter to the debtor in order to inform him of the delay and the amount owed. If the debtor does not subsequently fulfil this obligation the lender can terminate the loan agreement by notifying him by extrajudicial notification. By the termination of the loan agreement the lender has the right to demand the total amount of the loan, with interest and costs, which according to usual contractual terms becomes due. The total amount is charged with default interest. Furthermore the lender announces the termination to the archive of data of economic behaviour TEIRESIAS.[27] Further, the lender has the right to initiate enforcement procedures, charging the borrower with his judicial costs.

However, during the crisis, it has been recognised in several judgments that the lender has the obligation to tolerate a reasonable default on monthly instalments (*moratorium, obligation de non petendo*), especially when the default is caused by a temporary financial inability of the debtor and the pursuit of the lender's claim would cause serious financial harm to the debtor.[28] This obligation stems from the good faith and business usages[29], which govern the enduring contractual relationship of trust between the credit institution and the consumer.

2. What are the requirements to initiate enforcement procedures against the consumer?

The requirement to initiate enforcement procedures against the consumer are the common requirements of enforcement procedure as far as debts are concerned, pursuant to Articles 904 et subs. of the Greek CCP. The creditor must have an enforceable instrument according to Article 904 in order to begin the execution procedure (this being a final affirmative judgment, arbitral award, notarial document, foreign enforceable instrument after being granted an exequatur under Articles 905, 906, 323 and 903 of the Greek CCP, validated compromise by a Greek court or payment order). The usual enforceable instrument of the lender is the payment order. According to Articles 915 and 916 the creditor's claim must be certain (independent of any condition or term) and cleared (fixed by quantity and quality).

3. What are the steps of such enforcement procedure?

First of all, the creditor demands from the competent court the issuing of a payment order under the Articles 623 et subs. of the Greek CCP. The creditor presents to the court his application, the private document which demonstrates the cause of the debt (the loan agreement), the amount owed and the extrajudicial notification of the termination of the loan agreement. After the payment order is issued, the enforcement procedure starts with a formal notice from the creditor to the debtor, inviting the latter to voluntary performance in three working days, otherwise threatening execution. This notice called *epitagi* |επιταγή|is is placed at the bottom of a certified copy of the enforceable instrument (called

26 see also Section XIII, Question 1b.

27 see under VII.

28 See the 15607/2012 case of First Instance Court of Thessaloniki which concerned credit agreement with an open account.

29 See articles 281 and 288 of the Greek Civil Code.

apografo |απόγραφο|, see Article 924 Greek CCP). If the debtor remains silent the creditor proceeds with the enforcement by giving an order (*entoli pros ektelesi* |εντολή προς εκτέλεση|, see Article 927 Greek CCP) to a bailiff who is the agent authorized to levy execution. The debtor has the right to proceed to the attachment of the debtor's assets (movable and immovable) leading to a public auction. The public auction of immovable assets must be held after forty days from the date of the attachment (see Article 998 Greek CCP). The authorised bailiff prepares an attachment report with the description of the asset and the date of the auction, which is notified to the debtor. Creditors other than the petitioning creditor are entitled to assert their claims (see Article 927 Greek CCP). The creditor of the mortgage loan shall be preferred over other unsecured creditors (the main exception to this being tax obligations which are preferred independently of any security). If there are multiple creditors with a mortgage on the property under auction the principle of time priority is applied; the creditor who had first registered a mortgage on the property shall be satisfied first by the amount raised from the auction.

4. Can the consumer raise substantive objections against enforcement?

Yes.

a. Which ones?

The consumer can raise various substantive objections concerning faults with the procedure, the validity or the existence of the debt, the validity of terms of the loan contract which are important for the specific case even concerning mortgage loans (meaning that Greek procedural law offers the debtor a wide variety of defence instruments, unlike Spanish procedural law as decided in the Mohamed Aziz Case), the validity of the enforceable instrument etc., depending on each case. The consumer raises his objection against the payment order and the execution procedure with the legal remedy of *anakopi* |ανακοπή|(Article 632 for the objection against the payment order and Articles 933-937 for the objection against the execution procedure, Greek CCP). The deadline under which the debtor has the right to raise his objection is set out in Articles 632 and 934 Greek CCP).

Furthermore, the consumer may raise various objections against the enforcement procedure (see *supra*). He may for instance raise the objection of abuse of the creditor's right based on Article 281 of the Greek Civil Code (226 BGB) which states that: "the exercise of a right shall be prohibited if such exercise obviously exceeds the limits imposed by good faith or morality or by the social or economic purpose of the right". The courts in several cases have accepted the objection of abuse of the creditor's right to initiate enforcement procedure in order to satisfy his claim. Abuse of right may be on hand if the lender has started the execution procedure, even though the borrower has already started procedure for indebted individuals of Law 3869/2010.[30] In other cases it has been held that a credit institution wrongly initiated the enforcement procedure. One such instance relates to the standard practice in case of default on monthly instalments which is that the bank's employees contact the debtor, usually by phone, and then send him a warning letter providing an extrajudicial notification. Only fifteen days later does the bank normally demand the publication of a payment order. However in one particular case the bank immediately started the execution procedure after the first delay in payment of monthly instalments and without any notification to the consumer or special reason.[31] The initiation of enforcement proceedings by the creditor may also be considered abusive when the amount of the debt is disproportionally low compared to the value of the property under attachment.[32] Further, in the context of the difficult conditions of the economic crisis many judgments have found the creditor's

30 See of the large number of judgements the cases 8817/2012 of First Instance Court of Athens and 5422/2011 of Magistrate Court of Athens .

31 See indicatively the case 13/2003 of First Instance Court of Nafplio.

32 See case 60/2004 of the First Instance Court of Mesologgi, which judged that there is an abuse of right if the attachment of an immovable property of value 102.700 euros is exercised for the satisfaction of a debt of 450 euros.

right to terminate the loan agreement by the first default of the monthly instalments abusive, when this action provokes a significant damage to the debtor compared to the benefit of the bank.[33]

Until the 31 December 2013 by virtue of Article 19 of Law 3869/2010 as amended by the Legislative Act of 4 January 2011, Article 46 of Law 3986/2011, the Legislative Act of 16 December 2011 and the Legislative Act of 18 December 2012, the auction of the main residence of the debtor is suspended. Furthermore, by virtue of the Legislative Act of 16 December 2011 and the Legislative Act of 18 December 2012 the auctions accelerated by credit institutions for debts which do not exceed the amount of 200,000 euros are also suspended until the 31 December 2013.

According to settled case law, the initiation of enforcement proceedings while this suspension of the auctions is in force, is considered by the courts as an abuse of right. However, representatives of the creditors' states and organizations ("TROIKA") insisted in October 2013 that such suspensions of enforcement proceedings ought to be brought to an end. Law 4224/2013 published on 31 December 2013, which applies to all debtors including merchants, provided the further extension of the suspension of the auctions of the main residence under strict conditions, including the value of the main residence (which must not exceed the limit of 200,000 euros), annual income (which must not exceed the limit of 35,000 euros), value of assets (which must not exceed the limit of 270,000 euros including the main residence) and the amount of bank deposits (which must not exceed the amount of 15,000 euros). The suspension of the auction is not automatic. If the debtor fulfils these conditions, he must file an application to the credit institution (until 28 February 2014 or two months after the announcement of the formal notice which starts the enforcement procedures) and the auction procedures of the main residence are suspended. In addition, the debtor is obliged to pay a reduced monthly instalment, which represents 10% of his monthly income. Eviction is suspended until the 31 December 2014.

b. What is the legal effect of such objections?

If the objections of the debtor are accepted by the court the enforcement procedure stops. If the objection concerns the payment order then the latter is cancelled. The consumer also has the right to file an application for suspension of the execution procedure until the court's final decision concerning the objections is handed down (Articles 632 Paragraph 2 and 938 Greek CCP). An application for suspension will be accepted only if it is judged as probable that the main application (the objection against the procedure, the *anakopi*) will be successful and that the enforcement procedure will cause irreparable damage to the debtor.

5. Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?

Yes. Article 388 of the Greek Civil Code (§ 313 BGB) provides that:

"If having regard to the requirements of good faith and business usages the circumstances on which the parties had based the conclusion of a bilateral agreement have subsequently changed on exceptional grounds that could not have been foreseen; and the performance due by the debtor taking also into consideration the counter-performance results in an excessively onerous change, the Court may at the request of the debtor and according to its margin of appreciation reduce the debtor' s performance to the appropriate extent or decide the dissolution of the contract in whole or with regard to its non-performed part".[34]

Article 388 of the Greek CC allows the heteronomous modification and adjustment of the contract under exceptional circumstances and strict conditions in exception to the rule *pacta sunt servanda*. The requirements of the application of Article 388 are: 1) bilateral agreement, 2) change of the

33 See question 1, see also case 208/2013 of Magistrate Court of Athens.

34 Translation of the Greek Civil Code by Constantin Taliadoros, Ant. N. Sakkoulas Publishers 2000.

circumstances on which the parties had based the conclusion of the agreement according to "good faith and business usages'', 3) the change occurred after the conclusion of the contract, 4) the change was caused by exceptional and unforeseeable events, 5) because of the change, the performance has become excessively onerous. It is supported both in the case law and in theory that additional conditions exist: 6) the absence of a counter agreement, 7) that the debtor is not in default and 8) the agreement has not been executed yet, at least partially.[35]

It is accepted in Greek legal theory that the adjustment in new conditions based on good faith (corrective function of good faith) is also possible in loan contracts. According to the wording of the provision, Article 388 of the Greek CC applies in bilateral agreements. A loan contract is considered by some authors as a unilateral contract,[36] because only the debtor has the obligation to repay the amount of the loan ("re-concluded" contract). In contrast the lending by the creditor to the debtor cannot be considered as an obligation. However, modern theory accepts that the interest-bearing loan is a bilateral contract, because the interest is the price for the amount lent. In any case, Article 388 Greek CC is a specialised statement of the general principle of good faith as expressed in Article 288 of the Greek CC ("A debtor shall be bound to perform the undertaking in accordance with the requirements of good faith, taking also into consideration business usages."

a. How is the term "unforeseen/unforeseeable events" defined?

Unforeseeable events as part of Article 388 of Greek Civil Code are events which do not arise in the normal course of things but which are caused by unusual circumstances whether they be physical, political, social or economic (e.g. an economic crisis[37], legislative changes, natural disasters, currency devaluation etc.). Article 388 CC thus applies in cases where the parties to the agreement could not have foreseen these unusual circumstances and justifiably believed in the stability of the circumstances. The unforeseeable events are not identical to *force majeure*. The unforeseeable change in circumstances must lead to a significant disruption of rights and obligations of the parties to such an extent that the performance of the debtor becomes excessively onerous.

b. If adjustment is possible, what are its legal effects?

A court, which applies the regulation of Article 388 of the Greek CC, decides on the judicial correction of the contract. The adjustment of the agreement is valid for the future (after the filing of the action). The Judge is called on to restore the imbalance of rights and obligations of the contract by reducing or increasing the debtor' s performance to the appropriate extent, determined by the circumstances and the good faith, or in exceptional cases by deciding the total or partial dissolution of the contract. Although Greek law does not place an obligation on the parts to renegotiate the terms of the contract before the *ultimum refugium* of the judicial adjustment of their agreement, Greek theory supports such an obligation according to the general principle of good faith.[38]

The application of Article 388 of the Greek CC in credit agreements has not been generally accepted by the courts to date, although the majority of theorists are in favour of this.[39] The majority of the

35 Stathopoulos, Law of Obligations, (Σταθόπουλος, Γενικό Ενοχικό Δίκαιο), Σάκκουλας Αθήνα-Θεσσαλονίκη 2004, p. 1231.

36 see article 806 of Greek CC.

37 e.g. for the current economic crisis as an unforeseeable event see the decisions of the First Instance Court of Athens nr. 219/2014 and First Instance Court of Thessaloniki nr. 1180/2014, both of which concern the reduction of the agreed rent in contracts of hire of immovable property. See also the decision nr. 3627/1997 of the Court of Appeal of Athens for the economic crisis of that period (concerning also the reduction of the agreed rent in contract of hire of immovable property).

38 Karampatzos, Unforeseen change of circumstances in the bilateral contract, (in Greek) 2006, p. 493.

39 With the exception of some few but important cases, such as 5025/1990 Court of Appeal of Athens. See Doris, The judicial conformation of the content of contracts in periods of economic crisis (in Greek: Δωρής, Η δικαστική διάπλαση του περιεχομένου εκκρεμών συμβάσεων σε περιόδους οικονομικής Κρίσης) ΧρΙΔ 2012, 241 επ., Dellios, Still on-going

judgments which apply Article 388 concern contracts for the hire of immovable property (especially commercial leases) and ultimately reduce the amount of the payments to be made to the creditor. The application of this provision in credit agreements could lead to their reconsideration and adjustment in periods of economic crisis and over-indebtedness of consumers, in the form of the reduction of the interest rate, the extension of the schedule of monthly instalments, the obligation of tolerance of the delay (*moratorium*) etc.

A few decisions recognise that in a period of economic crisis the bank has the obligation, arising from the principle of good faith, to refrain from measures of relentless prosecution of the debtor (enforcement procedures) and to tolerate delay in payment and to offer repayment facilities (grace period or extension of the repayment time). The violation of such obligations may lead to the bank's liability for compensation to the debtor (decision Court of Appeal of Athens nr. 5025/1990, First Instance Court of Thessaloniki nr. 15607/2012).

6. *Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?*

With regards to the frustration of contract/purpose Greek theory and practice also accept the application of Article 388 of Greek CC.[40]

7. *Do the banks use private companies that deal with the recovery of debts with the result that legislation on consumer protection doesn't apply anymore?*

Unlike Romania, banks in Greece do not use private companies to deal with the recovery of debts.

VI. National legal framework applicable for over-indebtedness

1. *What are the possibilities for consumers in case they are considered "over-indebted"?*

The main law covering 'over-indebted' consumers is Law 3869/2010 as amended by subsequent laws. No previous law dealt with individuals' ('non merchants') bankruptcy. Where the consumer is considered over-indebted and provided the conditions laid out in Law 3869/2010 are met[41], the consumer can use the following possibilities:

- Mediation and out of court settlement (Articles 2 and 7 of Law 3869/2010); 42
- In-Court compromise/settlement, or
- Judicial debt settlement (re-organisation) which may even lead to discharge of the debt.

   a. *Is there the possibility for the consumer to reorganise debt or obtain debt relief?*

(Contd.)

banking credit contracts in periods of economic crisis (in Greek: Δέλλιος, Εκκρεμείς τραπεζικές πιστωτικές συμβάσεις σε περιόδους οικονομικής κρίσης) ΧρΙΔ 2012, 246 επ., Mentis Defence and Release of the over-indebted debtor, Dikaio kai Oikonomia P.N. Sakkoulas (2012), p. 1. [in Greek: Μεντής Γ., Άμυνα και Ελευθέρωση του Υπερχρεωμένου Οφειλέτη: Η πορεία προς μια νέα σεισάχθεια στα όρια μεταξύ αστικού δικαίου και νέου πτωχευτικού δικαίου, Δίκαιο και Οικονομία Π. Ν. Σάκκουλας (2012), p. 136 g.g..

40 For the interpretation of this article see question 5 above.

41 The material scope of Law 3869/2010 comprises debts of individuals who do not have the legal capacity to declare bankruptcy (according to mercantile bankruptcy law) and who have, through no fraudulent intention, permanent inability to pay back their debts. According to article 1 of law 3869/2010, debts that have been undertaken during the last year before the submission of the discharging application, as well as debts stemming from illegal acts committed by fraudulent intention, administrative fines/sanctions, fines, tax/debts due towards the State and Organizations of Local Authorities, Public law corporate bodies charges and contributions towards social security funds, are excluded from the scope of the provision.

42 According to law 4161/2013, the Out of Court Settlement is not any more a prerequisite in order to proceed with the petition. Out of Court Settlement was replaced by a discretionary mediation procedure.

Although the term 're-organisation' is not included in the law at issue, debt relief can only be allowed upon the initiation of the private persons' bankruptcy procedure as described in Law 3869/2010 which regulates the discharge of debt of over-indebted individuals (see supra).

i. How are the terms re-organisation and debt relief defined?

These terms are not defined in the relevant law. Although the Greek Insolvency Code refers quite often to a 'reorganisation plan' in case of merchants' insolvency, the term not only is it not defined therein, it can also be misleading, 'since a plan can be confined to provide only for alternative ways to liquidate the business without any measures of reorganisation'.[43]

ii. What are the requirements for re-organisation and relief? [see also under f) this section]

Requirements

Law 3869/2010 distinguishes between private (non-merchants) and commercial (merchants) bankruptcy[44] and provides that in order for individuals to benefit from discharge of their debts (either partial or total), they have to be permanently unable to meet their financial obligations, that is to be bankrupt. In other words, bankruptcy, as also defined for insolvency in the case of merchants, is a prerequisite for the consumer to benefit from Law 3869/2010, dedicated to the over-indebted natural persons. Greek Law does not distinguish between debt relief and debt discharge. However, as it requires the permanent inability on behalf of the individuals to meet their financial obligations it, in principle, demands that the individual is "bankrupt". However for a form of debt relief see the procedure of Law 4161/2013 under (e).

The requirements for the application of Law 3869/2010 are specified in Article 1. The first paragraph of this provision stipulates that persons that cannot file for insolvency ('non merchants'), provided they are permanently unable to meet their financial obligations as they become payable (i.e., they stop making payments, a test identical to that for merchant insolvency), they may benefit from Law 3869/2010. The requirements for application are: a) the debtor is a natural person (legal persons are excluded), b) unable to file for insolvency as defined in Article 2 of the Insolvency Code (that means that the merchants are excluded from the scope of application of the Law, even in relation to consumer or mortgage loans), c) permanent inability to pay debts, d) the debts have become due the absence of fraud in relation to the imputation of financial inability (e.g. transfer of assets). The fraud does not concern the time of the conclusion of the loan agreement (unless the consumer concealed economic data in order to misguide the creditor with regards to their creditworthiness), but rather relates to the time of the imputation of financial inability.[45] There are also some negative requirements: the second paragraph of Article 1 excludes from the scope of application of Law 3869/2010: a) debts that have been concluded during the last year from the filing of the relevant application to the competent Magistrate's Court (in order to prevent malicious behaviour from the consumer who has intentionally concluded a debt and then demands the discharge of it), b) debts that arise from a tort or committed by fraud, c) administrative fines, penalties, public taxes and fees to the government and to local authorities, fees to public entities and contributions to social security organisations.

The procedure

43 E. Perakis, 'The new Greek Bankruptcy Code: How close to the InsO?', 2008

44 Although see the reference in Art. 15 of the given Law on the application mutandis mutandis ('where necessary') of the Insolvency Code.

45 See case 193/2012 of Magistrate's Court of Lavrio and case 10/2011 of Magistrate's Court of Athens. There is also a different opinion of part of judgements concerning the Law 3869/2010 according to which the decission of concluding a loan agreement burdens the consumer who has to be diligent and choose the proper credit contract (see case 1/2012 of Magistrate's Court of Florina). This latter opinion apparently ignores the obligation of the credit institutions to assess the creditworthiness of the consumer (see under IV).

The debtor seeking discharge from his debts has to submit a petition to the local Magistrates' Court (Article 3 Law 3869/2010). Before the amendment brought about by Law 4161/2013, the debtor had the obligation to first attempt to settle out of court by sending his creditor a written request for extrajudicial settlement and by proposing a settlement plan with the obligatory assistance of a public entity (such as mediator from Banking Investment Services) or a lawyer. If that attempt failed, the debtor had six months to initiate court proceedings by submitting a petition for discharge of this debt to the Magistrates' Court. In practice, 99.9% of extrajudicial settlements failed. Therefore, after the amendment of Law 4161/2013 extrajudicial settlement is replaced by the term prejudicial settlement which is a non-obligatory procedure. As a result, the debtor may directly submit a petition to the court.

The petition to the Magistrates' Court must be accompanied by:

- A list of the debtor's assets and income, as well as the income of the debtor's spouse;
- A list of all creditors and their debts, divided into principal, interest and expenses;
- A debt arrangement plan that will reasonably balance creditors' interest with the debtor's assets, income and marital status;

Additionally the debtor can also submit:

- A statutory declaration that the lists of property and creditors provided are correct; and
- Every relevant document about property, income status, creditors and claims.

If a creditor is not included on the list of creditors, their claim is not affected by the process. On the day of the submission of the petition two hearings are set. The first hearing concerning the petition must be set within six months of its submission. However, due to the workload of the Courts, in practice the hearing is never set within six months. The second hearing is set within two months from the submission. At this hearing the Judge will verify the outcome of the settlement (if such a settlement took place) or will decide on the request for temporary injunctions according to Article 781 of the Greek Civil Procedure Code (if requested by the debtor). Until the time of the hearing the enforcement or execution measures are suspended. Additionally the debtor has to pay an amount that corresponds to 10% of the instalments due to all creditors on the day of the submission of the petition (not less than €40 per month).

The debtor must serve the petition to all creditors, which in Greece can be costly and thus may make the procedures less attractive to insolvent individuals. Service of the petition does not interrupt the accrual of interest on secured claims (contractual interest rather than default interest applies), unlike for unsecured claims, where interest accrual is interrupted by that service. Creditors have two months from service to provide their comments on the plan. The law provides for a presumption of consent to the plan for creditors that fail to comment.

iii. How many consumers have had debt reorganised?

According to unofficial information of the Courts,[46] approximately 5,000 decisions have been issued (since June 2011 when the law was first applied[47]), which have reorganised individuals' debts by reducing monthly instalments and interest rates, offering a grace period, and excluding the main residence from the liquidation of the assets. However, this is a very low percentage compared to the total number of petitions for debt re-organisation (100,000 petitions are now pending). This can be contrasted with the fact that up until June 2013 44,262 applications had been filed in all local Magistrates' Courts of Greece.

iv. How many consumers have obtained debt relief?

46 Based on interviews with judges and court clerks.

47 see under iv.

Since Greek Law 3869/2010 on the regulation of debts of over-indebted non-merchants (households) was only issued in 2010 (before 2010 there was not a legal framework on the insolvency procedures of non-merchant individuals) and since debt discharge requires the payment of monthly instalments determined by the Court's decision for a period of three to five years,[48] there has not been a discharge of debt to date. After the payment of instalments for this period of three to five years (four years in the majority of cases), the Court issues a decision which declares the debt discharged. The Greek Courts do not recognise the possibility of discharging the debt in advance under the condition of the payment of the instalments for the specified time period. Since the first decision which applied the procedure of Law 3869/2010 was issued in June 2011 (Magistrates' Court of Athens no. 15/2011), the first discharge of debt will probably be declared in the summer of 2015.

b. What are the requirements for initiating bankruptcy proceedings for consumers?

See the analysis under 1. a. (ii) of this section.

c. Is there a possibility for consumers to attain discharge of debt (Restschuldbefreiung)49 within bankruptcy proceedings?

Yes. The discharge of debt can be attained either through an agreement between the creditors and the debtor on the debt adjustment or settlement ('quasi-re-organisation of debt') or discharge (Article 7 of Law 3869/2010). Discharge of debt can be also achieved through a Court judgment (Article 8 of Law 3869/2010) which does not require the consent of creditors. The court can thus proceed to judicial debt settlement which can in some cases result in complete discharge of debt. Law 3869/2010, in harmony with the German Insolvency Law (*Insolvenzordnung*), provides that the Court may, after it has taken into account the debtor's income (personal and family) as well as his and his family's needs, request the debtor to pay monthly instalments for three to five[50] years according to the court's judgement (and not six as German law stipulates) a specific amount which will be distributed to the creditors evenly (Article 8 (2) of Law 3869/2010).[51] The given amount can be re-adjusted/reorganised following a new judicial ruling initiated by anyone who has a legitimate interest to do so.

The amount to be paid by the debtor to the creditors, as ordered by the Court, varies between very small amounts (sometimes even 'zero' sums *('Nullplan')*) if the debtor faces serious unemployment (not attributed to the debtor's liability), health or other serious problems, such as serious financial distress that prevents him from having any income (Article 8 (5) Law 3869/2010). According to Article 1 (3) a debtor can benefit only once from the discharge of their debts.

i. How is discharge defined in the national context? (Is there a definition?)

The equivalent term for discharge of debt (*Restschuldbefreiung)* in Greek Law is *απαλλαγή* [apallagi]. Neither the Insolvency Code nor Law 3869/2010 specifically define this term. At a conceptual level it is argued that,[52] under the influence of German Law, the debt is not completely discharged but remains as an 'incomplete (natural) obligation/non enforceable legal right'[53] (ατελής ή φυσική ενοχή). However, Article 11 of Law 3869/2010 provides explicitly for the full release of the debtor from his

48 Before the amendment of the Law in 2013 the period was 4 years.

49 Discharge of debt shall refer to the partial or total forgiveness of debt during or after completed bankruptcy proceedings.

50 Article 8 par. 2 of the Law 3869/2010 was amended by Article 16 of Law 4161/2013 (before the amendment the period of monthly installments was set at four years).

51 See for instance Cases 2/2011 and 4/2011 of Magistrate' s Court of Patra and case 15/2011 of Magistrate' s Court of Athens.

52 See Kritikos, Regulation of over-indebted physical persons' debts (in Greek: Κρητικός, Ρύθμιση οφειλών υπερχρεωμένων φυσικών προσώπων), 2nd edition, 2012 p. 247, Stathopoulos, Regulation of over-indebted physical persons' debts (in Greek: Σταθόπουλος, Ρύθμιση οφειλών υπερχρεωμένων φυσικών προσώπων) ΧρηΔικ 2011, p. 181, Spiridakis/Georgiakakis, Regulation of over-indebted physical persons' debts (in Greek: Σπυριδάκης/Γεωργιακάκη, Ρύθμιση οφειλών υπερχρεωμένων φυσικών προσώπων) 2nd edition, 2012 p. 101.

53 Similarly the provisions of the French Code de Commerce (L 622 – 32, L 643 – 11).

financial obligation and does not leave any space for considering the remaining debt as a non-enforceable legal right.[54] According to Article 11 (1) of Law 3869/2010 the discharge of debt concerns even creditors that have not put forward their claim.[55] According to Article 20 of the Constitution of Greece, as well as the 1 Protocol of ECHR, no discharge of debt can be considered without having given previously the right to the creditor to be heard.[56]

ii. If discharge is possible, after how many months/years is it possible?

According to Law 3869/2010 the debtor is considered debt free after complying with the three to five years payment schedule, which starts from the issue of the court's judgment and its notification to creditors. Although the law in Article 4 mentions that the hearing is determined within six months from the date the application is filed, in practice, because of the congestion of litigation procedures, the date of the hearing is usually set many years in the future (in some cases as late as 2024).

iii. If discharge is possible, what are the requirements for discharge?

If the debtor complies with the three to five years (depending on the court's judgment) repayment schedule ordered by the Court, they will be discharged from all remaining debt against all creditors (Article 11(1) Law 3869/2010). If the debtor delays payment in more than three consecutive months or if he repeatedly exhibits a 'negative attitude'57, the Court can order the removal of the debtor from the previous settlement, upon the application of one of the creditors. The discharge is ascertained or certified by the Court after the debtor has repaid the last instalment and the Court has issued a Declaration (declaratory judgment) (Article 11 (1) Law 3869/2010). In case of non-compliance of the debtor with the terms of the Court's decision, the creditors' claims are established again to the amount they were before the discharge (as if the discharge petition has never been submitted to the court).

iv. How many consumers have obtained debt discharge?

As mentioned above (under 1.a.iv) no discharge of debt has yet been declared, since the Law 3869/2010 and its application are very recent.

d. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

According to the Law 3869/2010, the debtor is considered debt free after complying with the three to five years payment schedule, which starts from the issuing of the court's judgment and the notification of the creditors. Although the law in Article 4 mentions that the hearing is determined within six months from the filing date, in practice, because of the congestion of procedures, the date of the hearing is usually set many years in the future (in some cases as late as 2024).. This phenomenon not only complicates the legal process but also deprives the law of its effectiveness. The over-indebtedness and financial inability of the debtor should be examined swiftly, as it is a situation of emergency, which may change dramatically within ten years. The only solution for the debtor is to seize the opportunity given by the law to request temporary injunction according to Article 781 of the Greek Civil Procedure Code. The injunction shall temporarily regulate the case by indicating a monthly instalment (at least 10% but not less than €40 with the exception of special circumstances of

54 For a discussion on this see Mentis G. Defense and Release of the over-indebted debtor, Dikaio kai Oikonomia P.N. Sakkoulas (2012), p. 1. [in Greek: Μεντής Γ., Άμυνα και Ελευθέρωση του Υπερχρεωμένου Οφειλέτη: Η πορεία προς μια νέα σεισάχθεια στα όρια μεταξύ αστικού δικαίου και νέου πτωχευτικού δικαίου, Δίκαιο και Οικονομία Π. Ν. Σάκκουλας (2012), p. 182 et seq.

55 As announcement here, it is considered the creditor's participation in the process of the debt settlement/re-organization.

56 This is expressed in Article 4 (6) of Law 3869/2010: ' if a creditor is not included in the lists of Art. 4 (1), his claim is not affected by the procedure, which starts for this particular creditor with the submission of the application as provided in par. 1.' (free translation).

57 By negative attitude it is meant the intentional non repayment although the debtor has the ability to pay.

great economic weakness, unemployment etc.), prohibiting enforcement measures and any change in the legal and factual situation of the debtor's property.

Furthermore, where the debtor owns immovable property which is used or may be used as his main residence, he has the opportunity to exclude it from the liquidation of his property (Article 9 of the Law). Where the debtor demands the protection of his main residence, the court shall decide the payment of a percentage of up to 80% of the "objective" value according to the tax authority during a period of 20 to 30 years (if the loan agreements last more than 20 years), with the possibility of a grace period. The debtor shall pay this amount in monthly instalments preferably to the secured by mortgage creditors. Consequently, the whole duration of the procedure for consumers owning their own homes, may even exceed thirty years.

e. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can have recourse to? Please list and elaborate on requirements, legal consequences, and numbers of consumers who have gone through the measures in question.

Law 4161/2013[58] introduced the 'facilitation scheme for performing borrowers' (Πρόγραμμα Διευκόλυνσης για Ενήμερους Δανειολήπτες). The provision applies only to debts arising from housing or credit or 'repair' loans that have a mortgage lien to the primary residence of the debtor.

The debtors or borrowers that can benefit from this provision must be natural persons and specifically, unemployed, pensioners, salaried persons of the public and private sector and the persons having an employment relationship under private or public law. The conditions for inclusion in the facilitation scheme are the following:

- The loan must have a mortgage lien on the principal residence and should not be terminated;
- The objective value of the principal residence must not exceed the amount of €180,000;
- The objective value of the total immovable property must not exceed the amount of €250,000;
- The total unpaid capital of the debt must not exceed the amount of €150,000;
- The total value of the deposits and the securities may not exceed the amount of €10,000.

Under this 'facilitation scheme' the monthly repayment instalment of the loan is reduced to 30% of the monthly individual or family income. The period for which the measure can be used is up to 48 months and while the current contractual rate applies, the difference that arises in comparison to the conventional 'new' instalments is capitalised and repaid after the grace period. The unemployed beneficiaries have, in addition to the previous advantages, the possibility to not pay any instalments, or any interest for up to 6 months within the grace period. Some special cases of borrowers can benefit from a monthly instalments with interest rate equal to the ECB base rate plus a margin of 0.75%, unless the contract specifies a lower interest rate.

The debtor can benefit from this provision only once and during its application, any legal and judicial measures on behalf of the bank are suspended and forbidden. The possibility of being included in the facilitation scheme was provided for 6 months from the publication of the Ministerial Decision (on 15 July 2013), this deadline has, however, been extended for three more months.

2. Is there a national legal or policy framework for avoiding evictions?

Until the end of 2013 there were two moratoria on evictions. Until the 31 December 2013 by virtue of Article 19 of Law 3869/2010[59] the auction of the main residence of the debtor was suspended. Furthermore, by virtue of the Legislative act of 16 December 2011 and the Legislative Act of 18 December 2012 the auctions arranged by credit institutions for debts which do not exceed the amount

58 ΦΕΚ 143Α / 14.6.2013.

59 as was amended by the Legislative Act of 4-1-2011, by the article 46 of Law 3986/2011, by the Legislative Act of 16-12-2011 and by the Legislative Act of 18-12-2012.

of €200,000 euros were also suspended until the 31 December 2013. According to settled case law, the initiation of enforcement proceedings while this suspension of auctions is in force is considered by the courts as an abuse of right. Specifically, this Legislative Act (Article 5) on the 'suspension of auctions for 2013' as published in issue A' of the Official Gazette of the Hellenic Republic 246/18.12.2012, provides that all (immovable) property for debt to banks less than €200,000 and the main or primary residence of any debtor, regardless of the debt - as long as the objective value of the property does not exceed the minimum taxable limit of primary residence - increased by 50%.

Law 4224/2013 provided the further extension until the 31 December 2014 of the suspension of the auctions of the main residence under strict conditions.[60]

In general, two cases shall be distinguished:

- Eviction of lessees in case of non-payment of rent

The term 'express eviction' has been regularly deployed in the news following Law 4055/2012 on a 'fair trial' which introduced the 'express' procedure for eviction of tenants who have not met their financial obligations. According to the relevant law the tenant has fifteen days to pay the debt or rent owed upon receipt of the lessor's out-of-court notification. If the lessee does not comply then the lessor can file an application for an eviction order. The time the Court needs to rule on the application varies depending on its workload, but an average estimate is two weeks. If the application is successful then the tenant has fifteen days to file a request for suspension of the eviction. Twenty days after the Court's decision has been delivered to the tenant (and provided that the tenant's defence has not been successful), the tenant can be forcefully evicted.

- Seizure/confiscation of immovable property and, in particular, primary residence

Article 14 (11) of Law 2251/1994 (on consumer protection) provides that no seizure of immovable property that constitutes the debtor's sole residence is allowed for debts arising from consumer credit and credit cards, as long as the debtor exercises his right to oppose the Court's enforcement order within fifteen days of receipt of notification. Cumulative additional conditions attached to the 'non seizure' provision are: a) the bank's claim does not exceed the amount of €10,000; b) no mortgage agreement exists with the given bank; c) the debtor is without intention unable to meet his financial obligations.

In accordance with the general law on consumer protection, Article 9 of the more specific Law 3869/2010 makes reference to the protection of the primary residence of the debtor. The law provides, on the one hand, that part or all of the property may be liquidated for the debtor to meet his financial obligations. However, under Article 9 (2) the debtor can submit a petition to the Court asking that his property that serves the role of his primary residence may be exempted from disposition. The law provides that where the only property of the debtor is his primary residence, his debt will be discharged as long as the amount of the debt to the banks exceeds 80% of the objective value of the property (Article 9 (2) of Law 3869/2010). This case should be distinguished from the case described under VI.1 lit e, and the discharge of debt as provided upon the fulfilment of the conditions of Article. Article 11(1) Law 3869/2010.

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (i.e. debt relief)?

When the 'home' at issue constitutes the primary residence of the debtor and the latter has exercised his legal rights in accordance with the relevant procedures (see above, under 2), they can remain in their home during the bankruptcy proceedings.

60 See analytically under V, question 4 a.

b. Is there a possibility for persons affected to stay in or move back into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

No such possibility is provided under Greek Law.

VII. The regulation of credit bureaus

1. How many credit bureaus are there in the country?

In Greece there are no credit bureaus of the type found in other countries. In a broad sense, several bodies could be characterised as a credit bureau such as the Credit Consolidation System (CCS or "white" TEIRESIAS), the Default Financial Obligation System (DFOS or "black" TEIRESIAS) and the Mortgages and Prenotations to Mortgages System (MPS) of TEIRESIAS Bank Information Systems SA.

2. Are the credit bureaus public or private?

The system of TEIRESIAS was founded in 1997 by the Union of Greek Banks. TEIRESIAS was originally founded as a non-profit corporation but since September 1997 operates as a société anonyme (SA).

If there are both public and private credit bureaus:

a. How many credit bureaus are public and how many are private?

TEIRESIAS is a private société anonyme. The biggest Greek banks are shareholders of TEIRESIAS.

b. Do the public and private credit bureaus have different functions and / or procedures? Are they concerned with the same data?

There are no other systems or credit bureaus in Greece.

3. How are credit bureaus compensated?

The system of TEIRESIAS is funded by the institutions that use it. The amount of the compensation depends on the use, on the number of searches that the institution makes.

4. How do the credit bureaus collect data?

The data are channelled to TEIRESIAS SA via electronic means or channels by the banks, leasing companies, companies providing credit, factoring companies, administrative card companies, the courts, the Registries of Deeds, the cadastral offices and the Ministry of Finance.

5. In what do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

The data included in the system of TEIRESIAS are personal and they are protected by Law 2472/1997 for the protection of personal data. The credit institution has the obligation to inform clients about the listing of their economic data in the system. However, the debtor's acceptance is not required (even for the listing in the "white" TEIRESIAS). According to Article 4 of Law 3816/2010[61] debts which do not exceed the amount of €1000 do not appear in the TEIRESIAS system. Furthermore, the period for which the data is retained has been decreased, for instance for the payment order from four to three years. By virtue of Article 3 of Law 3816/2010 the banks are obliged to immediately update the system of TEIRESIAS in case of debt repayment, in order to be deleted from the system.

61 which amended the corresponding articles of Laws 3259/2004 and 3746/2009 on the personal data processing

6. What data is collected by credit bureaus?

The Credit Consolidation System contains data concerning consumer and housing loans, credit cards of natural persons and credit to small and medium-size businesses (with annual revenue less than €2.5 million). It contains information about the status of the credit (current balance with no delinquency, delinquent balance etc.).

The Default Financial Obligation System contains data concerning bounced checks (the data refers to the drawer of the cheque), unpaid (at the time of maturity) bills of exchange, termination of personal/consumer/housing loans, termination of credit card contracts, termination of overdraft contracts, termination of leasing contracts, filings for bankruptcy, conciliation procedures (Article 99 Insolvency Code, see analytically under section XV), adjudicated insolvencies, issued orders of payment, fillings for debt adjustment and discharge (L. 3869/2010), liquidation auction announcements, forfeitures and checks of the 1923 Presidential Decree, debt adjustment judgments (e.g. Law 3869/2010), orders for the restitution of use of leased property and administrative sanctions against tax law violators.

Furthermore the Mortgages and Prenotations to Mortgages System contains data regarding mortgages, prenotation of mortgages and conversions of prenotation to mortgages.[62] Both DFOS & MPS aim at supporting a more accurate assessment of the financial credibility of the clients (current or future) by the banks.

7. Who are the users of credit bureaus?

The users of the systems of TEIRESIAS are mainly the banks in order to be facilitated in screening and monitoring borrowers as well as to avoid giving loans to high-risk individuals and to assess their creditworthiness. By virtue of the Article 12 of Law 2472/1997 on the personal data protection, every person has the right to access the system in order to know about personal data concerning him.

(Over-)indebtedness of consumers

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country? Elaborate.

The demand for real estate in Greece (especially houses) was always high due to the general preference of Greek people to own their house (the percentage of home ownership in Greece is 75%). Generally speaking, the price of real estate (not only houses but also other immovable property) were always on an increase. However, during the decade between 1996 and 2006 the price of real estate rapidly increased. This rapid increase has been "corrected" as a result of the crisis as, under techno-economic studies, during the period between 2009 and 2014 the price of real estate has decreased by a between 40 and 50%.

2. What is the relation between housing prices and over-indebtedness?

a. How have housing prices developed since 2000 (or later if earlier data not available)?

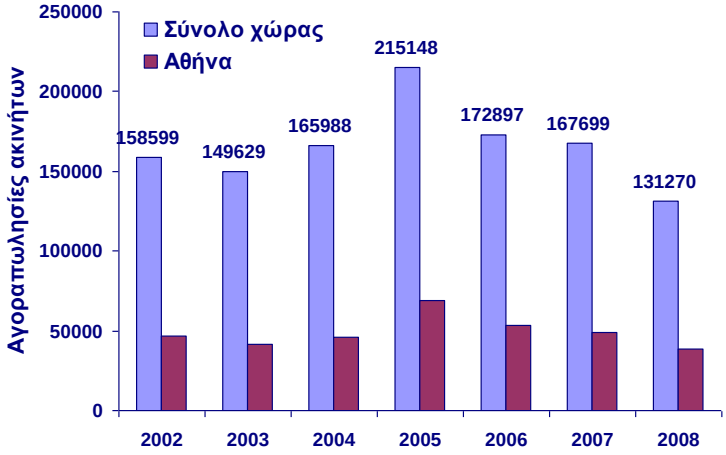
62 Mortgage prenotation is a type of a provisional mortgage which can turn into a full mortgage when the claim of the holder of the prenotation right is recognized by a final court decision.

This Table 6 shows the Real Estate Price Indices in Greece between the years 1993 and 2013.

Urban Areas						
(1997=100)						
Year	Quarter				Annual Average	/ Change in %
	I	II	III	IV		
1993	…	…	…	…	…	…
1994	…	…	…	…	76.1	…
1995	…	…	…	…	82.6	8.5
1996	…	…	…	…	91.2	10.5
1997	96.2	98.2	100.2	105.4	100	9.7
1998	110.1	113.9	115.0	118.4	114.4	14.4
1999	120.4	123.6	125.3	128.8	124.5	8.9
2000	132.1	135.7	138.8	144.2	137.7	10.6
2001	150.5	156.1	159.5	164.0	157.5	14.4
2002	171.5	180.3	180.7	184.9	179.3	13.9
2003	188.6	187.5	189.0	190.9	189.0	5.4
2004	190.6	191.6	193.3	198.0	193.4	2.3
2005	205.2	211.6	216.9	224.1	214.5	10.9
2006	233.3	238.8	243.6	253.4	242.3	13.0
2007	254.1	256	258.8	260.2	257.3	6.2
2008	260.8	261	261.4	261	261.1	1.5
2009	250.3	250.7	248.3	250.1	249.8	-4.3
2010	247.2	241.9	234.1	232.5	238.9	-4.4
2011	232.4	229	224.5	217	225.7	-5.5
2012*	207.8	203.2	197.1	188.9	199.2	-11.7
2013*	184.5	179.4	…	…	…	…

Source: Bank of Greece based on data collected by the credit institutions (2006-onwards, apartments only) and weighted index according to the stock of houses in Athens and in other urban areas (up to 2005, all dwellings).

Furthermore the following diagram shows the number of sales of real estate in Greece from 2002 to 2008. As shown, the sales were increasing until 2005 and since then they have gradually decreased. The blue colour indicates the real estate sales in the whole country and the purple colour indicates the real estate sales in the city of Athens.



Source: Bank of Greece

b. How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available?

See under II, questions 4 and 5.

3. Has there been increased access to mortgage credit? In which way? For example: was access to consumer credit facilitated through legislation? Elaborate. And has access to credit become more restricted since the crisis? Elaborate. If possible provide data.

In general, we can observe a credit boom in consumer loans since the mid-1990s. Greek households could borrow more easily after the ceiling on consumer loans was first raised in 1994.[63] However, consumer credit was completely liberalised only after mid-2003, when the ceiling (of €25,000 per borrower and bank) on consumer loans and the corresponding limits for the subcategories of consumer loans were all abolished. This development partly contributed to the rapid increase in consumer loan growth rates and the corresponding loan-to-GDP ratio as Chart 1 demonstrates (see supra).[64] The 'peak' of the credit boom was the year 2009, during which the total number of loans to private parties reached the amount of €119.635 million.[65] The increased access to consumer credit can be attributed to four distinct factors:

- the liberalisation of the Greek financial sector and the removal of consumer credit restrictions which commenced during the 1980s and 'took off' in the beginning of the 1990s. In the period until 1994, the Greek financial system was heavily regulated as interest rates were set at administered levels and credit was channelled to the economy through investment requirements imposed on banks as regards the financing mainly of the public sector and a complicated reserve/rebate system as regards the financing of the private sector. As a result of the latter, the loan interest rates received by banks were different from the rates charged to borrowers but also it was more profitable for banks to extend loans to enterprises than to households (mainly through mortgages).[66] In addition, this liberalisation triggered a higher demand for loans by firms and households that were previously effectively credit constrained.
- The 'easy lending' on behalf of the Greek banks and the poor control of the candidate borrowers. According to a report of the 'Association of employed consumers' (''Ενωση Εργαζόμενων Καταναλωτών Ελλάδας) there are many examples of extreme imbalances between the maximum borrowing capacity of the consumer and the reckless lending behaviour of the banks. Indicatively, the report notes, there have been cases, in particular in the rural areas of Greece, where banks granted loans of €250,000 to consumers with an annual (declared) income of €9,000.[67]
- The environment of falling interest rates, reflecting the process of convergence towards the levels of EU interest rates and the disinflation process in Greece;[68] and

63 Voridis, H., Angelopoulou, E., Skotida, I., 2003. Monetary policy in Greece 1990-2000 through the publications of the Bank of Greece. Bank of Greece Economic Bulletin No. 20, 7-86.

64 S. Brissimis, E. Garganas and S. Hall, 'Consumer Credit in an era of financial liberalisation: An overreaction to repressed demand?', Bank of Greece Working Paper 148, October 2012, p. 11.

65 EKPOIZO report, *ibid.*

66 Ibid, p. 11-12.

67 http://www.gsee.gr/userfiles/file/2013_BOXES/2013_10_17_%20eeke_statistika.pdf

68 *Ibid*.

- The formation of expectations by banks, consumers and firms of higher future incomes, associated with the benefits from the adoption of the euro in Greece, which led to fast growth in consumption and greater willingness to lend and borrow.[69]

Source: Bank of Greece

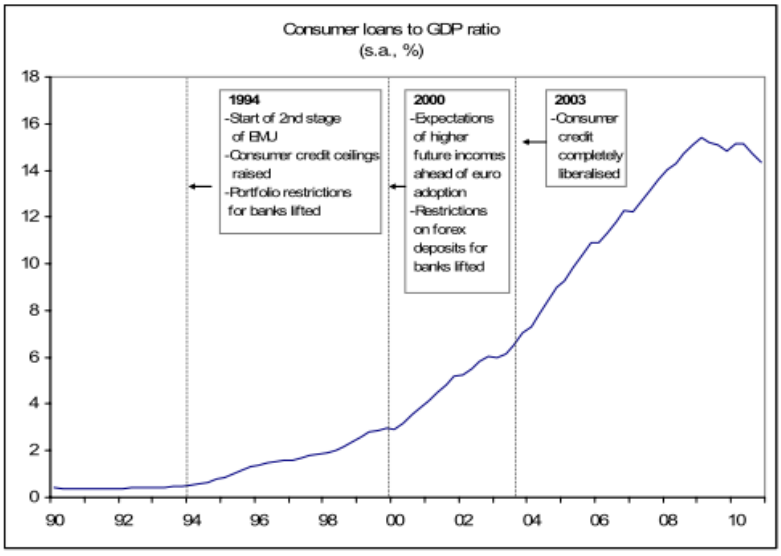
Since the crisis erupted, access to credit has indeed become more restricted. In 2010 we observe a decline in the granting of new loans.[70] In the period 2009-2010, despite the fact that lower ECB policy rates passed through to both business and mortgage loan rates, consumer loan rates did not follow suit. In this loan category, the greater importance attached by banks to credit risk and the rising ratio of non-performing loans led to an overall tightening of credit terms and conditions.[71] Consumer lending in Greece was virtually non-existent in 2013, as gross lending towards consumers (and also businesses) hit an all-time low.[72] The decline in the granting of loans to individuals can be attributed to the following factors:

Greek banks face major liquidity problems which declined further after the events in Cyprus and the banks' involvement in the PSI (private sector involvement, reduction of the public debt through the writing-off of 53.5% of the face value of Greek governmental bonds). Even after their recapitalisation in May 2013, which strengthened their capital base, Greek banks still could not provide loans.[73]

The rapidly increasing rate of non-performing loans (from mortgage loans to credit cards). In this context, the focus of Greek banks is on refinancing old loans, portfolio rationalisation, keeping NPLs from increasing further and making problematic loans serviceable again.[74]

The disposable income of consumers due to the ongoing austerity measures has undermined both the demand side but has also made more 'cautious' the supply side.

Chart 1



69 *Ibid.*

70 For more details see the provided Tables under Section II Question 4

71 *Ibid*, p. 14.

72 http://www.euromonitor.com/consumer-lending-in-greece/report. According to the same report: 'The only consumer credit category remaining active in 2013 was the so-called green loans, mainly for home energy-saving projects.'

73 *Ibid.*

74 *Ibid.*

4. What is the relation between employment and over-indebtedness?

a. How many per cent of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when

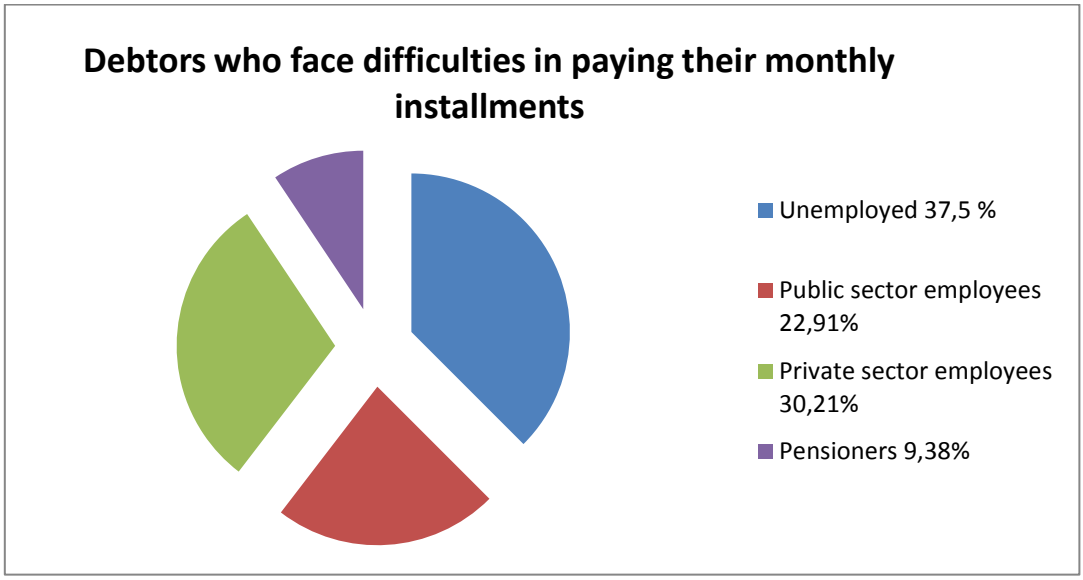
i. the credit contract was signed

70% of the consumers were employed and 30% were unemployed when the credit contract was signed.[75]

ii. over-indebtedness arose?[76]

As it was mentioned above under section II,[77] 35% of over-indebted consumers are unemployed and 65% of them are employed. More specifically 26% are employees of the private sector and 17.5% employees of the public sector. 17% of the over-indebted are pensioners, 1% are municipal employees, 1% are farmers and breeders and 5.3% do other professions. 6.5% of the over-indebted individuals are self-employed. Approximately 10% of the over-indebted individuals are partially-employed.

The same percentages were slightly different in 2009, according to the Annual Report of Economic and Social Statistics of VPRC:



b. How has the average salary evolved since 2000?

The OECD dataset contains data on average annual wages per full-time and full-year equivalent employee in the total economy.[78] We observe the 'peak' of the annual wages in 2009 and in 2012 we notice similar levels to the wages of 2006. The table, however, omits to take into account the higher taxation that stemmed – to a large extent - from the Memoranda of Understanding imposed by the creditors of the state. In addition to this, the table does not show the remarkable reduction in salaries in the public and private sector during the last two years. In the public sector, the salaries which before

75 Data from interviews with bank clerks.

76 According to the statistics of the Association of Greek Employed Consumers (October 2013) (http://www.gsee.gr/userfiles/file/2013_BOXES/2013_10_17_%20eeke_statistika.pdf)

77 question 5c, iii

78 Source: OECD, http://stats.oecd.org/#

2010 exceeded the amount of €2,000 have now been almost cut in half. Generally speaking, the average Greek person has faced a reduction of 35-50% in his monthly income.

Table 7

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
1	13852	14247	15863	16899	17.751	18.606	19.569	20285	20.973	22.120	21.048	20.542	19.807
2	19482	19.517	21178	21829	22.281	22.587	22.970	23.096	22.918	24.009	21.961	20.731	19.807
3	25635	25.680	27.866	28722	29317	29.720	30.224	30.390	30.156	31.591	28.897	27.279	26.063
4	25049	25.093	27.229	28066	28647	29.041	29.533	29.695	29.466	30.869	28.236	26.655	25.467

1. Current prices in National Currency Unit (NCU)
2. 2012 constant prices and NCU
3. 2012 USD PPPs and 2012 constant prices
4. 2012 USD exchange rates and 2012 constant prices

5. *Non-EURO countries: Did national monetary policy play a role in consumer credit and mortgage agreements?*

   a. *Are/were foreign currency loans common?*

Even though Greece is a EURO-country, loans (especially housing-mortgage) in Swiss francs (CHF) were very common in Greece between 2006-2009. The credit institutions proposed loans in CHF due to their favourable terms (low amount of monthly instalments and low interest rates). According to 2501/31-10-2002 Act of the Governor of Bank of Greece the credit institution is obliged to properly inform its clients about the risks arising from probable exchange rate fluctuation in foreign currency loans. This kind of information was, however, absent in the majority of loan contracts in CHF.

   b. *What are the foreign currencies in which loan agreements were concluded?*

In CHF.

   c. *Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?*

Yes, they are. The exchange rate of CHF and Euro in 2007 was 1.65, while today it stands at 1.23. Now, when consumers or borrowers request settlement of their loans issued in CHF, the credit institutions accept it under the condition that the contract in CHF is replaced with a new contract in euros but on the basis of today's (for consumers) unfavourable rate. As a result, the debts of consumers who concluded loans in CHF, have now almost doubled. For instance (an actual case is cited as an example):

LOAN AMOUNT IN CHF (2007)	EXCHANGE RATE CHF-EURO	LOAN AMOUNT IN EUROS (2007)
420.859,80 CHF	1,65	255.066,54€
CURRENT LOAN AMOUNT IN CHF (AFTER REPAYING FOR 4 YEARS)	EXCHANGE RATE CHF-EURO	CURRENT LOAN AMOUNT IN EUROS
396.450,45 CHF	1,22	324.959,38€
FINAL ADDITIONAL CHARGE AGAINST THE DEBTOR BECAUSE OF THE CHANGE IN THE EXCHANGE RATE		69.892,84€

If the exchange rate was still 1.65 the debtor would now owe the amount of €240,273. This means that the debtor is additionally charged with the amount of (€324,959.38 - €240,273) €84,686.38 euros because of the change in the exchange rate. After repaying for four years the debtor still owes more money than the initial loan amount in 2007.

6. *Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?*

The biggest macro-economic risk factor in Greece for the time being and for the next years is – according to our perception- the dramatically high level of unemployment, which exceeds the official statistic of almost 30% of the active population (more than 50% of young people of the age of 20-30). A great number of debtors who had a job during the conclusion of the loan contract are now facing the serious problem of no (or reduced) income, while they are obliged to repay fully the instalments of the loan. Otherwise they are charged with interest for late payment-default interest, which may reach the high rates of 12-15% for consumer loans and more than 17-18% for credit cards.

IX. Micro-economic risk factors for over-indebtedness (consumer behaviour).

1. *What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)*

As shown in Table 2 (Loans to households divided by loan type, in millions of euros, 2007-2013[79]) under question 2 of part II (see also above), the majority of credit agreements concluded from 2007 to 2012 are mortgage and housing loans. The amount of the money given by virtue of mortgage and housing loans is approximately twice the amount given by virtue of consumer credits (consumer loans, credit cards etc.)

These statistics show that the main reason for a consumer to take a loan is to buy or build a house. Renovation loans are also frequent. As far as the consumer credit is concerned, many consumers concluded a consumer loan in order to buy a car with ownership retention (this means that the bank retains ownership of the car and the debtor has only the right to use it until the whole debt is paid).

During the period of prosperity in Greece (between 1997 and 2007) the credit institutions offered a variety of consumer loans, such as loans for vacation, loans for consumption during Christmas etc.

Tables 2 and 3:[80]:

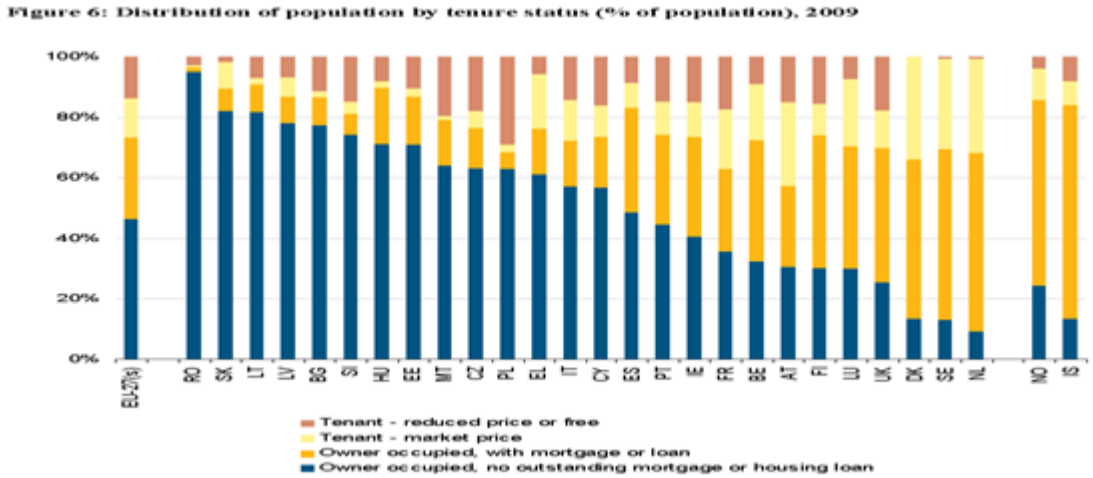
Percentage of loans with reference to the type of the loan

Loans of over-indebted households	Percentage per type of loan
Consumer loans	48.79%
Credit Cards	28.87%
Housing Loans	19.87%
Business Loans	1.1%
Refinancing Loans	0.49%
Overdraft facilities	0.49%
Open credit loans	0.27%
Joint accounts	0.11%

79 Source: Bank of Greece, 'Bulletin of Conjunctural Indicators', Issue 153 November-December 2013 (Τράπεζα της Ελλάδος, «Στατιστικό Δελτίο Οικονομικής Συγκυρίας», Τεύχος 153 Νοέμβριος-Δεκέμβριος 2013)

80 According to the statistics of the Association of Greek Employed Consumers (October 2013) (http://www.gsee.gr/userfiles/file/2013_BOXES/2013_10_17_%20eeke_statistika.pdf)

Percentage of loans with reference to the total amount of the loans



Loans of over-indebted households	Percentage per amount/value of loan
Housing Loans	61.68%
Consumer loans	31.25%
Credit Cards	4.98%
Business Loans	1.42%
Open credit loans	0.27%
Refinancing Loans	0.25%
Joint accounts	0.09%
Overdraft facilities	0.06%

2. *How many credit agreements do consumers conclude on average?*

Each borrower (if employed) has debt on average in 3.56 banks. The average number of loans (consumer credit and mortgages) for each borrower is 4.43 loans.[81]

3. *Was/is the housing market in the country based on rent or ownership?*

The percentage of ownership in Greece is high. According to the statistics of Eurostat in 2009, 75% of Greek people owned their home. 60% of the Greeks live in their home without a mortgage loan and 15% acquired their own home with the help of a mortgage loan. According to Eurostat, Greece ranks 16th in Europe with regard to ownership.

Source: Eurostat: "*Housing conditions in Europe in 2009*"

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if available)? Please provide absolute numbers AND percentage as of population/home owners/indebted consumers/over-indebted consumers.*

81 http://www.gsee.gr/userfiles/file/2013_BOXES/2013_10_17_%20eeke_statistika.pdf

Loans to households (divided by loan agreement, in millions of Euros), 2007-2012:[82]

Year	Total Number of Loans	Change In %	Mortgages	Change in %
2007	104.116	22.2%	69.363	21.5%
2008	117.203	12.60%	77.700	11.2%
2009	119.635	3%	80.559	3.7%
2010	118.120	-1.2%	80.507	-0.3%
2011	113.050	-3.9%	78.393	-2.9%
2012	106.530	-3.8%	74.634	-3.4%
2013*	101.349	-3.5%	71.493	-3.2%

*Until November 2013

See also the tables 2 and 3 under question 1 of the current section.

5. How many indebted and over-indebted consumers have credit card debt?

According to a research of the Department of Statistics of Athens University of Economics approximately 80-90% of the indebted and over-indebted consumers have credit card debt (see above, section II, questions 4 and 5).

a. How high is this debt?

According to a research of the Department of Statistics of Athens University of Economics, the credit card debt of the Greek consumers in 2009 reached 10 billion euros.

b. How long does it take consumers on average to repay credit card obligations?

No such data is available.

6. How many per cent of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?

0.5% of the loans to over-indebted persons are overdraft facilities (see above under question1, table 2). EKPOIZO's research shows that in 2012 one in three consumers (38%) delayed the repayment of his monthly consumer credit and credit cards, whereas in 2009 the percentage was only 13.4 %.

a. How high is this debt?

According to statistics offered to the newspaper "Kathimerini" by the Vice President and General Director of Visa Europe of Greece Nikos Kampanopoulos, in September 2008 the amount of money withdrawn with the use of overdraft facility reached €2.2 billion. This debt has gradually decreased, as in 2009 it was €1.7 billion and in 2010 €1.2 billion.

b. How long does it take consumers on average to repay overdraft facility debt?

No such data is available.

7. How long does it take consumers to repay overdraft facility obligations?

No such data is available.

8. Is there a relation between the length of the credit obligation and over-indebtedness?

82 Source: Bank of Greece, 'Bulletin of Conjunctural Indicators', Issue 153 November-December 2013 (Τράπεζα της Ελλάδος, «Στατιστικό Δελτίο Οικονομικής Συγκυρίας», Τεύχος 153 Νοέμβριος-Δεκέμβριος 2013)

a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*

Due to the great variety and the diversity of contractual terms of the various credit agreements it is hard to precisely define the relation between the length of the credit obligation and the phenomenon of over-indebtedness. Consumer credit is typically shorter in length than mortgage loans which may be up to 40 years. In credit obligations which are short in length the monthly instalment amount owed by the consumer is higher. This fact may lead the consumer to repayment difficulties. However, it can be stated that the consumer cannot predict his economic situation in the long term and plan his life accordingly. Since the crisis, many consumers even have faced difficulties in repaying loans taken in the 1990s.

b. *How long are the time periods for which consumers took on credit and mortgage obligations? Is there a difference in data from before and after the crisis?*

The time periods of mortgage obligations are on average from 10 to 40 years. The time period of other credit obligations depends on the type of loan, the amount of lent and the amount of the monthly instalments. Consumer credit obligations have a time period of 2 to 10 years. No difference in data is observed in relation to the crisis.

c. *What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?*

It is hard to estimate the time that passes between the conclusion of a loan agreement and the default of the agreement, as it depends on the causes of the default. For instance, the economic crisis led to salary reduction and to increase of unemployment. As a result, many indebted consumers started having repayment problems in relation to their credit obligations, regardless of their duration. As far as loan agreements with short period are concerned, the monthly instalments are higher and in case the consumer has not made planned properly and also has other loan obligations they are more likely to breach the contract.

X. Relation between income and (over-)indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

A survey conducted by ΙΜΕ ΓΣΕΒΕΕ (in collaboration with the company MARC AE) from a sample of 1207 representative households in Greece during December 2012 provides the following data. The reduction in consumer spending is remarkable in all areas. In particular the clothing industry has suffered the most since 92.5 % of households have cut clothing expenditure. Similarly, approximately 93% of households have reduced spending with regard to the catering industry, while approximately 88% of households have decreased expenses for cinemas and coffees. Approximately 70% cut expenses on general food consumption.

The following table depicts the reduction in consumption by income class.

	Up to €10,000	€10,001-18,000	€18,001 – 25,000	€25,001-30,000	More than €30.000
Food	79.1	73.7	61.1	59	35.1
Alcohol/Cigarettes	56	50.9	51.7	44.9	33.8
Furniture/Electronic Devices	71.5	73.4	71.9	67.9	59.7
Transportation	80.9	80.7	75.4	82.1	66.2
Heating	87.3	85.2	81.8	80.8	61
House Bills	76.1	74.7	60.6	66.7	45.5
Health/Medicines	35.1	26.1	21.7	23.1	13
Education	16.3	16.3	13.8	12.8	3.9
Clothes/Shoes	93.1	94.2	92.1	94.9	81.8
Restaurants	93.6	94.2	93.6	91	84.4
Cafes/Bars/Cinemas	90.1	90	88.7	88.5	75.3
Travelling	90.1	91.2	88.2	88.5	76.6
Gifts	90.1	93.5	90.6	89.7	74
Bread/Bakery Products	75.8	70.7	68	71.8	44.2

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

No.

   a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate this risk through higher interest rates?) (Do low-income consumers pay more interests for mortgage agreements than high-income consumers?)*

As a rule, no higher interest rates are imposed by the lenders on low-income consumers in order to mitigate the (existing) default risk (See however also next question, under b).

   b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

Although, as aforementioned, no such (income-based) differentiation exists, it is likely that low-income consumers fail much more often than high-income consumers to meet their contractual/credit obligations. This will eventually result in interest charged for late payments (τόκοι υπερημερίας) which will increase the total amount low-income consumers pay.

   c. *Are there other key terms which change according to the income of the borrower?*

The borrowing/credit limit is reduced for low income borrowers, both in quantitative terms – number of loan agreements- and in qualitative terms – amount of credit in a single loan agreement.

In case of default, the debtor may apply to the bank in order to agree for a settlement of the loan (such as reduction of the instalments, lengthening of the loan, interest rate reduction, grace period-moratorium etc.). In order to examine the application the bank demands the debtor's payroll attestation and tax declaration. The terms of the settlements are more favourable for debtors who have low income. Many credit institutions offer very favourable settlements (e.g. low monthly instalments) for unemployed debtors.

Behaviour of actors in relevant cases

XI. Irresponsible lending practices[83]

1. Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)

In most cases, consumers are attracted by the advertisements of the credit institutions publish in media. During the period of growth of consumer credit in Greece (the decade before the economic crisis of 2008), the credit institutions were taking the initiative for the conclusion of loan agreements by informing consumers about lending programs by telephone or by letter. The intermediary between the consumer and the bank is a bank employee.

2. Was a creditworthiness assessment undertaken before granting the credit?

Before Directive 2008/48 on credit agreements for consumers and the Common Ministerial Decision (CMD) Z1-699/2010, which implemented it in national law, in many cases the creditworthiness assessment was imperfect. Often, the creditworthiness assessment was totally omitted by the credit institution. For instance, there are cases in which the credit institutions were giving credit to persons with low or no income such as students (see case 7241/1999 of First Instance Court of Athens, in which the bank agreed to provide a guarantee on a debt of €18,500 for a 19 year old with no income and no property).

a. In how many cases were creditworthiness assessments undertaken?

A statistical answer is impossible. However, between the years 2000-2010 it is observed that the level of the creditworthiness assessment was obviously insufficient.

b. Who was the initiator of the creditworthiness assessment?

The initiator of the creditworthiness assessment was always the bank.

c. Who undertook the creditworthiness assessment?

The responsible department of the bank assesses the creditworthiness of the consumer.

d. What were the criteria of the creditworthiness assessment (empirics)?

The criteria of the creditworthiness assessment are the income and the assets of the consumer (his economic status in general), the existence and amount of other credit agreements. The credit institution checks the total debt burden of a candidate borrower in relation to his income. This percentage must not exceed 30-40%. Another criterion of the creditworthiness assessment is the existing customer relationship between the bank and the consumer. The existence of a payroll account or deposit account is now in the top of the list of positive criteria in the final assessment process.[84] The means used for the assessment are documents about the economic status and the assets of the consumer (information sheet completed by the consumer, payroll attestation, tax declaration, declaration of real estate).

e. Was a credit bureau involved?

The responsible bank's employees also check the archive of data of economic behaviour TEIRESIAS, in order to check the existence and amount of loan agreements between the consumer and other credit institutions ("white" TEIRESIAS). In addition through this database, the credit institutions can check

83 The information provided is based on the experience of the legal and banking practice. They have been interviewed: a) representatives of four consumer organisations, b) representatives of law firms which are specialised in this field, c) bank employees from the four Greek systemic banks which are active in the Greek market.

84 Information provided by banking employees and clients of credit institutions.

the existence of bounced checks, insolvency petitions and their evaluation, of delays in other loan repayments, payment orders, seizures and auctions, mortgages and their possible removal, terminations of loan and credit card contracts and the administrative penalties against violators of tax laws ("black" TEIRESIAS[85]).

3. *Is there a legal obligation for a mandatory creditworthiness assessment? Is this obligation observed in practice? How are the criteria for creditworthiness assessment in legal provisions?*

The legal obligation of creditworthiness assessment is based on Article 8 of the CMD Z1-699/2010 (implementation of the Directive 2008/48). According to Article 8 of the Directive 2008/48 and of the CMD Z1-699/2010) "before the conclusion of the credit agreement, the creditor assesses the consumer's creditworthiness on the basis of sufficient information, where appropriate obtained from the consumer and, where necessary, on the basis of a consultation of the relevant database."

The legal consequence in case the credit institution "violates its obligations according to paragraphs 1 and 2 of this article" is the total discharge from the total cost of the credit including interests. The *ratio* of the provision (the prevention of over-indebtedness of the consumer) reveals the mandatory character of the creditworthiness assessment.

In addition to this, Article 27 Paragraph 3 of the Greek Banking Law (Law 3601/2007) provides that: "In case of application for a loan or other credit by a credit or financial institution, the applicant shall provide complete and accurate information for the assessment of his solvency and creditworthiness. Credit and financial institutions have the obligation to take into account in the rating of the risk under this article, any partial or total refusal of the applicant to provide such information. The information does not include sensitive personal data under the legislation''. This article reveals the importance of creditworthiness assessment for the whole banking system and its proper function.

4. *Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?*

There is no data available. There is no data available either concerning the reasons for credit refusal. Consumer organisations, when interviewed, referred to credit given even to consumers with very low income, despite the fact that the consumers had expressly declared their insufficient incomes and properties.

5. *Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?*

In the majority of the cases, the creditor does not explain to the consumer the consequences of failure to comply with the monthly payment obligations, unless the consumer asks so. However, the average consumer is not familiar with the legal terms usually used by the creditor (e.g. payment order). Many consumers ignore the exact legal consequences of the default of the loan agreement (such as the high default interest rate) due to incomplete information.[86]

6. *Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?*

The only way the consumer could have felt 'pressured' by the lender would be through indirect pressure of some misleading advertising regarding the lending conditions, as well as through some aggressive 'distant selling' practices adopted by the banks to promote loans and credit cards, in particular over the phone. In fact the First Instant Court of Athens has repeatedly ordered the removal of advertisements that mislead consumers, in particular by announcing a low interest rate (for instance

85 see analytically under section VII

86 Information based on interviews with representatives of consumer organisations. .

4.97% for one year), while the Annual Percentage of Actual Costs (ΣΕΠΠΕ) appeared on screen as rolling and in very small letters.[87]

There have been also reported many cases in which the lender pressed the debtor to sign a refinancing loan in order to repay already existing debts and forced debtor' s relatives to sign as guarantors under the threat that if they do not comply with this, the credit institution will proceed to enforcement procedures on the debtor's assets.[88]

XII. Irresponsible borrowing practices – emphasis on mortgage

1. *Did the consumer read the agreement before signing?*[89]

The overwhelming majority of consumers do not read the agreement before signing.

2. *Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?*

In over 90% of the cases no.[90]

3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*

In over 90% of the cases no. [91]

4. *How much time did the consumer take before signing the agreement?*

As a rule, less than 1-2 minutes.

5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

Consumers almost never make use of their right to withdrawal. The withdrawal period in Greece ranges from 10 to 15 days. According to the Article 14 of the Directive 2008/48 and the CMD Z1-699/2010 the consumer has a period of 14 calendar days in order to withdraw from the credit agreement without giving any reason. That period of withdrawal begins (a) either from the day of the conclusion of the credit agreement, or (b) from the day on which the consumer receives the contractual terms and conditions and information in accordance with Article 10, if that day is later than the date of the conclusion. In that case, the consumer has two obligations: a) to notify this to the creditor; and b) to pay to the creditor the capital and the interest accrued thereon from the date the credit was drawn down until the date the capital is repaid, without any undue delay and no later than 30 calendar days after the dispatch by him to the creditor of notification of the withdrawal.

87 See for instance Cases 1212/2007 and 33/2008 of the Court of First Instance of Athens (Πολ.Πρωτ.Αθ).

88 Information based on interviews with with representatives of consumer organisations.

89 Data provided under this section were collected in interviews with 150 (one hundred fifty)consumers who have a bank loan as well as with 20 (twenty) bank employees. This data corresponds also to what is presented by G. Dellios, Standard Contract Terms, Sakkoulas 2nd edition (2013), p. 7 et seq. [in Greek: Γ. Δέλλιος, Γενικοί Όροι Συναλλαγών, εκδόσεις Σάκκουλα, 2013, σελ. 7 επ.)

90 From the 150 interviewed consumers 134 answered that they did not compare credit offers from other banks.

91 From the 150 interviewed consumers 136 answered that they did not ask for any explanation concerning the contract terms.

Litigation

XIII. Issues in litigation

1. Has there been litigation before national courts challenging the content of mortgage/other loan agreements?

After the enactment of Greek Law 2251/1994 on consumer protection (see Article 2 about the general terms and conditions, unfair terms, which implemented the UCT 93/13 on unfair terms in consumer contracts), the Greek Courts judged several cases about the validity of various terms of credit contracts and credit card contracts. The Greek case law is not as rich as the German one after the German AGBG (now §§ 305ss BGB). However, the Greek Supreme Court (Areios Pagos) has already set the basis for a complete check of the content of credit contracts (see below, under a and b).

a. What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?

The applicable law was Greek law. The emphasis was on contract law and banking law.

b. What were the issues in question? (ie: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)

The issues in question were indicatively:

- The meaning of "consumer" in Greek law 2251/1994 (Article 1 paragraph 4), the consumer is defined as the final recipient of goods and services. According to the wording and the object and purpose of the law, even a business firm can be the final recipient of a consumer loan. However, this issue remains controversial today. The number of judgements (e.g. case 940/2011 of the Greek Supreme Court) and of authors, who argue that the concept of "final recipient" should be interpreted (correctively) narrowly has increased.[92]
- The meaning of "significant imbalance" (see UCT 93/13). It is worth mentioning that for several years (from 1999-2007, after the amendment by Law 2741/1999) Greek Law on consumer protection (Article 2 Paragraph 6 of Law 2251/1994) only required "simple imbalance". After the amendment by Law 3587/2007 in 2007, the concept of "significant imbalance" was brought back. The Greek Courts (see in particular the cases 1219/2001, 430/2005, 2123/2009 and 652/2010 of the Greek Supreme Court) set as basic indicator (criterion) for the acceptance of unfairness of a term the significant deviation from jus dispositivum, which poses a fair distribution of burdens and risks between the parties.
- The control of the height of normal interest rate and interest rate for late payment (default interest rate)-according to the Article 2 Paragraphs 6 and 7 of the Law 2251/1994 (it is still a controversial issue, as it concerns the definition of the main subject of the contract or the adequacy of the price and remuneration, Article 4 § 2 of the UCT 93/13, see case 1219/2001 of the Greek Supreme Court). It is significant that even *the Aziz* case of the ECJ left this issue unsolved.
- Penalty for early repayment of house loans with a floating interest rate. These terms were judged as invalid according to the article 2§6 of the Law 2251/1994.[93] Subsequently after the amendment of Law 2251/1994 in 2007 (by Law 3587/2007), a subparagraph (λβ') was added to Article 2 §7 (non-exhaustive list of unfair clauses), according to which the terms which provide

92 Regarding the various views supported, see in German: Paparseniou, Griechisches Verbraucher-vertragsrecht, Sellier-European Law Publishers, 2008, p.11, Mentis, Zur nationalrechtlichen Ausdehnung des subjektiven Anwendungsbereichs von Privatrechtsrichtlinien, in Karakostas/Riesenhuber, Methoden-und Verfassungsfragen der europaischen Rechtsangleichung, De Gruyter, 2011, p. 117, 120s.

93 See case 430/2005 of the Greek Supreme Court.

compensation/penalty in favour of the supplier without the latter having the obligation to invoke and prove the loss that he suffered, are invalid.

- Clauses which charge interest before provision of the loan (these clauses were judged as invalid, according to the article 2 §6 of the Law 2251/1994[94]).
- Charge of various costs against the borrower or consumer, such as costs against the borrower or consumer for the examination of his application for granting a certificate about the amount of his liabilities.[95]
- Interest calculation based on a year of 360 (not 365) days (this term was judged as invalid[96]).

c. What were the predominant issues (before and after 2008)?

Since the beginning of the crisis and the increased inability of consumers to meet their financial obligations we observe a change in the predominant issues challenged before the Courts. Since the adoption of the law for the debt regulation of the over indebted consumers, we observe an increased recourse to the Greek Courts by the consumers who wish to benefit from the in court settlement (and out-of-court settlement) Law 3869/2010 provides for and all the issues that pertain to it (qualification, inability to meet obligations). In addition, we note an increase in the tenancy disputes and the applications for evictions filed by the landowners. With regard to contract law and consumer law we notice that more and more consumers seek refugee to the provisions relating to the abusive and unfair contract terms in order to challenge in particular their mortgage agreements, but also their credit loans and the relevant interest rates.

2. Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?

The plaintiffs were mainly organised groups of consumers (over 90% E.K.POI.ZO.).

3. What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?

No such data is available.

4. Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?

Yes.

If yes:

a. How are those interests defined?

The law provides the right of consumer organisations to file an action for the protection of the general interest of the consumers ("class action", syllogiki agogi, Art.10 §16 L-2251/94).[97] There is no specific definition of the interest of the consumers.

b. What are the requirements for such representation?

The consumer organization must have at least 500 members.

94 See case 2123/2009 of the Greek Supreme Court.

95 See case 961/2007 of the First Instance Court of Athens.

96 See indicatively case 430/2005 of the Greek Supreme Court.

97 see for this provision in German Beuchler in Micklitz/Stadler, Das Verbandsklagerecht in der Informations- und Dienstleistungsgesellschaft, 2005, 173s, 179 ss

5. *In practice, is litigation in "public / diffuse interest" more common than individual litigation?*

Concerning the application of Article 2 of Law 2251/94 (unfair contract terms) litigation in "public interest" is by far more common.

6. *Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?*

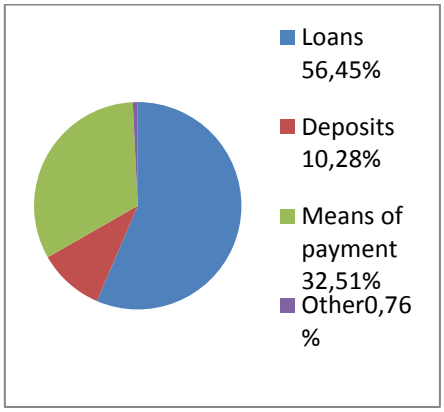
Yes. Due to the high cost of judicial proceedings, the consumers usually attempt an out-of-court settlement.

7. *Do consumers make use of out-of-court settlement procedures?*[98]

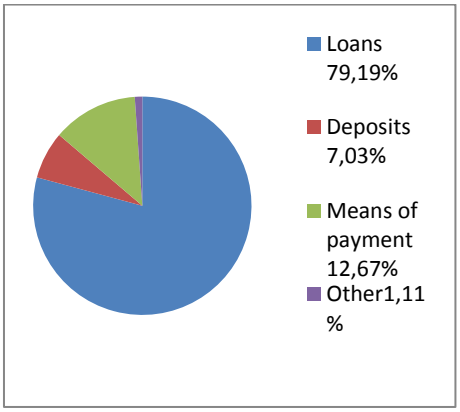
If yes:

a. *Which ones?*

Consumers often turn to relevant public institutions, such as the Ombudsman for Banking and Investment Services (OBIS, established in 2005) and the Consumer Ombudsman (established in 2004 by the Law 3297/2004). The majority of complaints, written or via telephone, concerns bank loans, as it is shown in this graph:[99]



Written complaints to OBIS



Telephone complaints to OBIS

b. *What is their success rate?*

During 2011, the OBIS examined 1,898 written complaints of which 1,472 were dealt with. In 417 cases the consumer was vindicated (28.3%), in 410 cases the bank was vindicated (27.8%) and in 645 cases a compromise was reached (43.9%). The grade of satisfaction of the consumers in relation to the compromise solution is up to 72.2%.

c. *What are the issues?*

The majority of the complaints concern loans, in particular the interest rates relating to loans and the terms of mortgage agreements. Many complaints further concern the 'indirect (not easily realised by the consumer) charges and surcharges' imposed by banks.

8. *Are there special bankruptcy courts? What is their role?*

98 All the statistics used come from the Annual Report of the Ombudsman for Banking and Investment Services for the year 2011.

99 Data from OBIS (Annual Report of the Ombudsman for Banking and Investment Services for the year 2011).

In Greece there are not special bankruptcy courts. According to the Article 4 of the Greek Insolvency Code the competent insolvency court for the declaration of insolvency is the First Instance Court in the district which is the centre of the debtor's main interests.[100]

XIV. Impact of the crisis on litigation

1. Has there been an increase in litigation since the financial crisis? And how many mortgage agreements were challenged in out-of-court or judicial proceedings before and after the crisis?

Data from the Greek Courts provide that there has been a tremendous increase in litigation since the financial crisis, in particular with regard to applications for judicial settlements in accordance with Law 3869/2010, which has caused huge delays in the administration of justice. We further observe an increased recourse to judicial proceedings on behalf of landlords who wish to evict their tenants, as well as by lenders who wish to challenge their mortgage agreements. We further observe an increase in the out of court settlements. According to data presented by ΕΚΡΟΙΖΟ (Ε.Κ.ΠΟΙ.ΖΩ) within the period between September 2010 and December 2012, 64,772 applications *for out of court settlement* were filed by consumer protection organizations to banks. Out of these applications only one was successful.

POMEK's (ΠΟΜΕΚ)[101] data shows that the phone calls to the Organisation's services (representing consumers) requesting out of Court settlement are approximately 100,000 per year, whereas the cases that address mortgage agreements are approximately 70% of the total number of cases. Members of POMEK alone filed 44,551 applications between September 2010 and December 2012 44.551.

According to ΕΚΡΟΙΖΟ, more than 34,000 applications for judicial settlement have been filed to the Magistrates Courts of the country (data from 1 January 2011 until 31 December 2012). Out of these applications 9,335 applications were filed to the Magistrates' Court of Athens, out of which one judicial settlement was successful, two out-of-court settlements were ratified by the Court, 85 decisions were issued by the Courts, 469 cases were considered admissible and were processed and 382 were dismissed as inadmissible. Until March 2014, according to unofficial data provided by ΕΚΡΟΙΖΟ, the number of applications pending in Courts all over the Greece has reached the 100,000 (the number of applications has doubled in almost one year).[102] For the rest of the country, data from other district courts show that the hearing of the case is likely to take place even later than the year 2024, leaving the adjudication of many mortgage agreements pending by the courts because of the huge workload.

As was mentioned above in section II, approximately 5,000 decisions have been issued which reorganise mortgage loans and other consumer loans (by virtue of the Law 3869/2010).

Unfortunately the data does not distinguish between mortgage agreements and consumer credit. With regard to the possibilities of out of court settlement for over-indebted consumers (Law 3869/2010) the following table is demonstrative of the low success rates of this type of settlement:

100 According to paragraph 2 of this article, center of main interests is the place where the debtor exercises the administration of his interests and which is recognizable to third parties. For legal persons it is presumed, until the contrary is proved, that the center of their main interests is the place of their registered office.

101 Πανελλήνια Ομοσπονδία Ενώσεως Καταναλωτών «Η Παρέμβαση» (National Association of Consumer Protection Organizations "Paremvasi")

102 This information has been confirmed to the authors of the Case Study by the General Secretary of the Ministry of Development.

Period September 2010 – September 2012[103]

Approximate total number of applications (for out of Court settlement in accordance with Law 3869/2010)	40,000
Number of applications (filed by the Greek Ombudsman and other consumer protection bodies)	22,220
Successful settlements[104]	5

For over-indebted consumers, Article 2(1) of Law 3869/2010 (after amendment in 2013 by Law 4161/2013) provides the possibility of recourse to mediation as an alternative to the filling of the application to the Court. However, this possibility has not yet been used.

Most cases are challenged under contract law or consumer law. The issues pertain to consumers' default as well general contract terms and abusive and unfair contract terms.

2. Did the Aziz ruling have an impact on national legislation / legal framework?

No. The main law for consumer protection; Law 2251/1994 has not changed since the Aziz judgment. Law 2251/1994 transposed Directive 93/13/EEC into Greek law and constitutes the main broad legal framework for consumer protection. Article 2 of the given law provides for an indicative list of unfair contract terms, whereas Article 2 Paragraph 7 provides a non-exhaustive list of specific contract terms that are deemed *ex lege* unfair, and as such, void and forbidden. The rules regarding the unfairness of contract terms specify the more general rule that exists in the Greek civil code, Article 281, according to which any abusive or unfair exercise of a right or an institution (in this case, contractual freedom) should be forbidden.

Regarding the Aziz case, the national legislation has no need of improvement or change. As indicated above,[105] the defence instruments of a debtor even in relation to a mortgage loan could also involve the invalidity of the terms of the loan agreement. Furthermore, the debtor could in any case apply for suspension of the execution, if his objections against the claim and the procedure are judged as probable to succeed. Furthermore, the Aziz case does not give - according to our opinion- a clear answer to the problem of high interest rate (ordinary or default interest rate). This will allow the Greek banking practice to continue applying high interest rates without any substantial control by the unfair contract terms Directive (93/13).

a. Are there cases before national courts dealing with issues that also arose in the Aziz case?

Currently we are not aware of any pending cases dealing with issues that also arose in the Aziz case (see also above section XIII.1). With regard to:

- The use of acceleration clauses in contracts planned to last for a considerable time – in this case 33 years – for events of default occurring within a very limited specific period, Greek courts have ruled that any contractual terms that allow the bank to terminate the credit agreement for no serious reason are unfair. Such 'not serious enough reasons' may consist in the delay by the consumer of payment of any of the instalments, or part of the instalments or interest.[106] In specific cases where the remaining debt is not very high ('σημαντικό')[107] and there are not sufficiently serious reasons proving the debtor's inability to fulfil his contractual obligations, the

103 Data from Geniki Grammateia Katanaloti (General Secretariat of Consumers)

104 "Successful" means that the credit institutions agreed to the plan of the settlement proposed by the debtor, including reduction of the monthly instalments, grace period etc.

105 question 4, under section V

106 ΕφΑθ 5253/2003 (2003) [Court of Appeals of Athens, Case 5253/2003]

107 The debtor had already paid 48 out of the 72 installments.

temporary inability to pay the monthly instalments does not provide for a sufficient reason for the termination of the account.[108]

- The unilateral establishment by the lender of mechanisms for the calculation and determination of variable interest (floating interest rate) – both ordinary and default interest – which are linked to the possibility of mortgage enforcement and do not allow a debtor to object to the quantification of the debt in the enforcement proceedings themselves but require him to resort to declaratory proceedings, in which a final decision will not be given before enforcement has been completed or the debtor will have lost the property: in long and medium term loans clauses of interest readjustment are frequent. According to ΕιρΑθ (Magistrate Court of Athens) 1896/2007 such clauses are not unfair as long as there is a legitimate interest for the interest increase and this increase is based on specific reasonable criteria. In other words, the clause has to be both reasonable and specific. In cases where the interest rate is subject to change unilaterally by the bank, without the client being aware of the criteria of this change, the bank is at breach of the clarity and transparency clauses, without a need to examine whether the practical application of this term has resulted in too harsh imbalances for the consumers (ΑΠ 1219/2001, Supreme Court 1219/2001). This term is unfair and thus void. Any term that allows the bank to increase unilaterally the interest rates without providing a specific and important reason that could justify this increase and without providing in advance the consumer with specific and reasonable criteria as to the potential increase, is unfair.

- The disproportionality as to the determination of default interest rates,[109] see Case ΕιρΑθ 1642/2008 (District Court of Athens Case No. 1642/2008)

b. What was / is considered an unfair contract term in the national court rulings before and after Aziz?

According to the First Instance Court of Athens (Judgment 711/2007)[110] in order to identify whether a general contract term is unfair, first it has to be examined whether the term constitutes a significant imbalance (in the sense of the deviation from the general understanding/practice, see under section XIII) and then to examine the degree of intensity of this deviation. Consequently, as a primary step, in order to establish whether a term disrupts the contractual balance between the two parties and is thus, unfair, the relationship of the balance of rights, obligations, and interests has to be specified and determined in each particular contractual form.

Article 2 (7) of Law 2251/1994 provides for an indicative list of 'per se' unfair (forbidden) terms, that is terms that are deemed automatically unfair without any further balancing of rights. In case the term does not fall within the enumeration of Article 2 (7), it is examined whether the general contract term at issue entails any deviation from evaluations/guidelines of soft law, namely the unfairness of the term will be judged according to the criteria of subsections a and b of Article 2 (6) of Law 2251/1994.[111]

Some examples of unfair contract terms before the Aziz case, as provided in the case law (an indicative list relating to loan agreements) are (see also under section XIII.1):[112]

Supreme Court, Case 1332/2012

108 EIP AΘ 208/2013 (2013) [Magistrate Court of Athens, Case 208/2013]

109 See Case C-415/11 Aziz [2013] ECR I-0000 par. 31 and 65 et seq., Case C-415/11 Aziz [2013] ECR I-0000.

110 Πολ. Πρωτ. Αθ. 711/2007 (2007)

111 Article 2 (6) of Law 2251/1994 provides that: 'General contract terms that have resulted in a substantial disruption of the balance between the rights and obligations of the parties, to the detriment of the consumer, are void and prohibited. The unfair character of the general term in a contract is considered after having taken into account the nature of the goods or services covered by the contract, its purpose, all the specific conditions existing at the contract's conclusion and all other terms of the contract or of another contract on which it is dependent.'

112 The list is far from being exhaustive.

- Terms that provide the termination of the credit agreement without a specific limit of overdue debts by the debtor.

Supreme Court of Greece, Case 652/2010

- Charges on credit cards for cash withdrawals from a branch or ATM of the same bank;
- €50 surcharge as costs of processing the request of the consumer for acknowledgment of debts and billing costs in order to examine a request for a single loan application and loan pre-approval (961/2007 ΠΠρΑθ);
- Charges on not recently used accounts and charges for maintaining accounts with a low balance;
- Notification by the bank of changes in contractual conditions and terms through leaflets or notices in stores;
- Exclusion of liability of the bank for fraud or gross negligence if the bank proceeds to a payment to a non-beneficiary before the beneficiary or owner notified the bank of the loss of the bank book;
- Delay of interest due on amounts that are deposited or withdrawn from another branch than the one of the account.

Court of Appeals of Athens, Case 3956/2008

- Bank commission when account movements per month exceed a certain number;
- Bank commission in cases of deposit of cash in favour of third parties that maintain an account in the same bank;
- Imposition of interest on the whole loan and not only for the amount that was released.

First Instance Court of Athens, Case 961/2007

- Credit card terms that retroactively charge contractual interest, that change the contractual interest only in cases of increase of the intervention, that charge for cash withdrawal;
- Terms in bank leaflets that charge for reviewing a loan request;
- Terms in savings accounts that allow the banks to change the interest depending on the balance of the account; or that move the beginning of interest due (valeur) to another day

First Instance Court of Athens, Case 6774/2003

- Terms that allow the bank to define the contractual interest accordingly (charging the customer's account) in case of partial repayment by the consumer (payment in instalments).

Court of Appeals of Athens, Case 5253/2003

- Terms that allow the bank to terminate the credit agreement in case of delay by the consumer of payment of any of the instalments, or part of the instalments or interest;
- Terms that allow the assignment of rents from immovable property to the bank;
- Terms that provide that in case of early repayment of the loan, the bank has to be compensated (unfair term as too imprecise against Article 2 (7) (ia) law 2251/94).

Supreme Court, Case 1219/2001

- Terms that allow the bank to impose on the depositor at its discretion costs for moving the account.
- Terms that allow the bank to unilaterally determine the interest rate.
- Terms which provide that only the Courts of Athens are competent locally to resolve disputes related to the credit contract.

- Terms which provide that unless the debtor contests the credit account balance within twenty days after the receipt of the monthly statement, it shall be deemed to have recognised and accepted the balance.
- Terms that allows the bank to demand from the creditor annual subscription, which is adjusted by the bank.

The patterns in the pre-Aziz national case law did not change after the Aziz judgment. In contrast, national courts continued basing their analysis on the general clause provided under Article 2 of Law 2251/1994, and the more specific clauses provided therein. Indicatively, the Magistrates' Court of Athens (Ειρηνοδικείο Αθηνών) ruled in Case 966/2013 that the term that allows the bank to proceed to a unilateral set-off declaration (entailing the money withdrawal or confiscation from the consumer's current account), but without notifying in advance the other party or consumer of this enforceable act is unfair.

c. Did Aziz have any other impact on national legislation / legal framework (ie. in the field of procedural law)? What are those impacts?

No.

3. Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework? Elaborate.

The increase of retail banking in Greece especially in relation to credit contracts led to the increase of judgments of Greek Courts which deal with cases of consumer credit and general terms of such contracts. Consequently the field of consumer credit and the problem of protection of consumers have largely occupied Greek legislation and jurisprudence since 2000 (see the amendment of Law 2251/1994 on the Protection of Consumers by Law 3587/2007). To date there has not been a CJEU case which has had a crucial impact on national legislation after the financial crisis.

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?

Not especially, there are only very few fragmentary regulations. For instance, by virtue of Ministerial Decision 2/19843/0094/7.3.2012, the obligatory assignment of six tenth of the borrower's salary or pension to the Deposit and Loans Fund (DLF) in order to repay the loan was reduced to 3/10. The borrower has the right to file an application to the DLF in order to demand the reduction of this obligatory assignment.

2. Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?

The legal field which experienced the most innovative changes after the economic crisis was bankruptcy law. Furthermore, Article 99 of the Insolvency Code was amended in 2011 by Law 4013/2011 which introduced the resolution procedure (which replaced the conciliation procedure) as a pre-insolvency stage. The resolution process is applied to all the merchants (physical or legal persons) who are or tend to be unable to pay their debts. The previous procedure only concerned big enterprises with importance for the whole of society. Further details of this change will be omitted given the emphasis of this study on consumers.

3. What are the changes in particular? Focus on consumer credit and mortgage law.

For the first time the "insolvency" of over-indebted non-merchants was regulated in Law 3869/2010 (which was amended in 2013 by the Law 4161/2013). This pioneering step by Greek law was due to the dire economic situation of many debtors because of the crisis (unemployment, reduction of salaries, over-indebtedness etc.). Despite the fact that the Law has only been in force for three years (since 2010), there are numerous judicial decisions. This led to the amendment of Law 3869/2010 in 2013 by Law 4161/2013, in order to resolve some problems of application of the law, to facilitate the whole procedure and to accelerate the regulation (even temporary) of the debtor's loans (see VI).

Another important, if temporary, legislative measure after the crisis was the suspension of the auctions of the main residence, which was extended until 31 December 2013 by virtue of Article 19 of Law 3869/2010 (as amended by the Legislative Act of 4 January 2011), Article 46 of Law 3986/2011, the Legislative Act of 16 December 2011 and the Legislative Act of 18 December 2012. Furthermore, by virtue of the Legislative act of 16 December 2011 and the Legislative Act of 18 December 2012 every auction arranged by credit institutions for debts which do not exceed the amount of €200,000 is also suspended until the 31 December 2013. These measures were taken in order to face the great number of auctions held, particularly by banks, and to protect the main residence of the debtor as an asset protected by the Constitution itself (Article 17 for the protection of the property and Article 21 for the protection of the family). By virtue of Law 4224/2013 the suspension of the auctions was further extended until the 31 December 2014.

Another important change in the field of consumer credit was the harmonisation of Greek law with Directive 2008/48 on credit agreements for consumers with the CMD Z1-699/2010. The CMD Z1-699/2010 implemented all the provisions of the Directive and among them the obligation of a creditworthiness assessment by the bank, the right of early repayment and the regulation for linked credit agreements.[113]

Furthermore, in summer 2013 a new regulation was introduced in the national law of mortgage credit. Law 4161/2013 (Chapter A) introduced the legal possibility of regulating mortgage loans, called the "Program of Facilitation of performing borrowers-debtors". This regulation is not an amendment or a variation of non/merchants' insolvency (Law 3869/2010) but is a new and independent legal path for borrowers who want to settle their loan. It is an extrajudicial procedure, a kind of *ex lege* settlement of the loan. Debtors who fulfil the strict conditions provided by the law have the right to request from the credit institution (creditor) a program of "favourable treatment of their debt" as it is described in the Law. If the debtor fulfils all the conditions, the credit institution has the legal obligation to accept the settlement. This regulation applies to the debtors filed an application until the 14 January 2014 (for six months after the date when the law came into force, 15 July 2013). It is a permanent measure with a limited practical effect.

The conditions of application of the Law are described analytically and in detail (Article 2):

- The Law applies only to mortgage loans with a tangible security on the main residence of the debtor (practically it concerns mainly housing loans).
- The loan agreement must have been concluded before 30 June 2010 (regardless of subsequent renewal or amendment).
- The loan agreement must not have already been terminated.
- The objective (taxable) value of the debtor's main residence must not exceed the limit of €180,000 (for debtors with three or more children this limit is up to €200,000).
- The objective (taxable) value of the debtor's total real estate must not exceed the limit of €250,000 (for debtors with three or more children this limit is up to €300,000).

113 Article 15 of the Directive and the Greek CMD: '' Where the consumer has exercised a right of withdrawal concerning a contract for the supply of goods or services, he shall no longer be bound by a linked credit agreement''.

- The total value of debtor's deposits and other transferable securities (e.g. shares) must not exceed the limit of €10,000 (for debtors with three or more children this limit is up to €15,000).
- The unpaid amount of the remaining capital of the loan (the settlement of which is demanded by the debtor) must not exceed the amount of €150,000.
- The debtor must be either i) unemployed, or ii) employee in public or private sector, or iii) a pensioner, or iv) a person who provides salaried services (a freelancer).
- The debtor's annual family income must not exceed the amount of: i) €15,000 for one person or ii) the amount of €25,000 for persons who undergo a joint tax return (e.g. married couple). These amounts are increased by €5,000 for families with 3 or more children and for debtors with a disability rate of 67% and more.
- The debtor's income must have decreased at least 20% from their income in 2009.

If one of the conditions is not met the application is dismissed.

Despite the complex conditions, the procedure is simple. The debtor files an application to the credit institution (creditor), which includes his full personal details and a demand for the grace period he wants to be given. Additionally, the debtor submits to the bank all the documents that prove the conditions described above and a declaration of honour about his income, assets, and debts. The credit institution must examine the application within 25 days and if the conditions provided by the law are fulfilled it has the legal obligation to accept it and to conclude a new agreement with the debtor.

This new agreement program of facilitation has a particular content described in the law. The program of facilitation gives the debtor a grace period of up to 48 months. During this period the debtor pays reduced monthly instalments of an amount equal to 30% of the debtor's monthly family income. This regulation does not lead to a reduction of the total loan or to a discharge. It is rather a reduction in the monthly instalments for a limited duration.

Only unemployed debtors have the right to demand to pay zero instalments for six months and to be relieved from payment of the interest for this period of the program (six months). It is important that during the program of facilitation the proceedings of the creditor against the debtor and the guarantors as well are suspended.

The credit institution has the right to terminate the program if the debtor does not comply with his obligations or if the latter is not sincere in relation to the amount of his income or the value of his assets (e.g. if data is deliberately hidden). In addition to this, the program terminates automatically if the debtor files an application of insolvency to the court according to the law 3869/2010.

The debtor can make use of this provision only once.

The criteria for application obviously have an economic as well as social basis (protection of unemployed, large families etc.). However, the conditions are complex and strict, meaning many over-indebted debtors are beyond the scope of application of the law. Additionally, this legislative regulation was criticised for excluding (implicitly) the merchants from its scope of application, as they are completely unprotected (the only exemption is the suspension of auctions of main residence which is terminated on 3 December 2013) in relation to their personal debts (such as housing loans) and their main residence.

Only 1,000 applications to the program of facilitation had been filed to banks by September 2013. This limited use of the regulation is due to the numerous and strict conditions (according to EKPOIZO the majority of debtors are left out of the scope of application because they do not fulfil only one of the conditions), the reluctance and delay in credit institutions examining the applications and the fact that the majority of debtors choose the legal path of insolvency (L. 3869/2010) which offers the opportunity to be freed from their debt.

4. *When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

The changes analysed above occurred after 2008. They are national policy initiatives in order to face practical problems (legal as well as social) caused by the economic crisis. Especially in relation to the consumer credit law, the changes occurred in compliance with EU legislation (Directive 2008/48).

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, ie with regard to savings?)*

Another phenomenon which has had an impact on consumer indebtedness due to the global crisis was the selling of risky financial products (repos, futures, options, swaps etc.). After the bankruptcy of the *Lehman Brothers* many Greek credit institutions (which also offer investment services) were forced to take responsibility for the selling of these products and the absence of proper information given to the investors. According to Article 25 of Law 3606/2007 (which imported Directive 2004/39 on markets in financial instruments) investment firms shall provide the proper information to their client according to their investing profile, experience and level of knowledge. Although this law does not provide any legal consequences for the non-performance of these obligations, it may constitute the conditions for an action based on tort according to Article 914 of Greek Civil Code[114] (equivalent to Article 1384 of the Civil Code). As a legal consequence the investment firm or the credit institution shall pay not only compensation to the investor, but also monetary reparation for "moral damages". In recent years after the bankruptcy of Lehman Brothers, many investors asked for judicial protection. For instance, in case 19932/2009, the First Instance Court of Thessaloniki ordered the bank to compensate €82,000 to the investor due to the absence of proper information before the selling of risky Lehman Brothers products (given that the inventor was a pensioner with little education and a lack of investment experience).

Furthermore, many Greek consumers in the last three years have deposited their money in Cypriot banks due to the fear that the Greek banking system will collapse. In the meantime, the Cypriot banking system collapsed which the consequence that many Greek depositors lost their savings and cannot pay their debts towards Greek banks.

114 Article 914 ''Meaning-A person who has caused illegally and through his fault prejudice to another shall be liable for compensation''.

PORTUGAL

Catarina Frade and Mariana Almeida

Preliminary information

The research team for this national report conducted several interviews with relevant actors in order to gather information concerning some parts of the questionnaire. We have tried to overcome the lack of statistical data for some parts and to collect the perceptions of some field players. We conducted semi-structured interviews based on the script of the project. We interviewed 29 consumers, four judges (two of first instance courts and two of appeal courts), two lawyers (one of them is also a member of a Consumer Defence Association) and an employee of one of the biggest financial institutions. We also made contact with Portuguese Central Bank (BdP) asking for more detailed statistics on indebtedness and credit default but we were redirected to the official data published by the BdP in its reports and website. The same happened with the Ministry of Justice contact. Other institutions like the Balcão Nacional do Arrendamento simply admitted the inexistence of more detailed and updated data. Finally our efforts towards financial institutions, including the association representing specialised credit institutions (ASFAC), were fruitless since they denied or were not able to provide us the required information.

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

Neither of the concepts is legally defined. However, they are commonly used in political and economic discourse as well as in public debate. The concepts were defined by socio-legal scholars (Marques et al, 2000) and adopted by other institutions without clarifying their understanding of the terms indebtedness and over-indebtedness.

According to socio-legal scholars Marques et al. (2000), indebtedness means the financial balance of a household, that is, the situation where a family has at least one credit commitment. If it has more than one credit the household is multi-indebted. Over-indebtedness represents the situation where a household is unable to meet its payments on time, most often its credit instalments.

A term used in the Portuguese legal framework is that of the consumer in a "harsh economic situation". It may be related to the term over-indebtedness but it does not coincide with it because it is narrower. The term was only introduced into the law in 2012, when new legal regimes were adopted to help households in financial difficulties. These regimes are described below.

Over-indebtedness is not a legal concept in Portuguese law. As such the definition of bankruptcy prescribed in the Bankruptcy Code (see below) is a more similar concept (yet still distinct) to that of over-indebtedness. For legal scholars, both terms are not synonymous. Usually bankruptcy refers to a judicial procedure and the condition of the individual that files for it, while over-indebtedness is a larger term and may exist even when consumers do not file for bankruptcy or when this procedure is unavailable to individuals. For instance, a household may be over-indebted because it lacks own financial means, but is still able to repay its debts thanks to financial support from relatives and/or friends.

2. Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?

The term "vulnerability" regarding consumers of financial services is not defined in the national law. Recently, however, two laws (Decree-Law 101/2011, of 30 September 2011 and Decree-Law 138-A/2012 of 28 December 2012) used the term "vulnerable consumer" referring to access to electricity and gas services. A vulnerable consumer is someone suffering from economic and social need that requires protection. More precisely it is a person that receives at least one of the following social benefits: i) solidarity supplement for the elderly, ii) "social insertion" income, iii) social unemployment benefit (a benefit that occurs after regular unemployment benefit for the most vulnerable unemployed people), iv) the highest level of child benefit, v) social pension disability.

3. Is the term "poverty" or "low-income consumer" defined in the national legal order?

Neither the term "poverty" nor the term "low-income consumer" is defined in the Portuguese legal order. The term "poverty" is regularly used in official statements in its technical sense (see, for instance, the Communication from the Commission EUROPE 2020- A strategy for smart, sustainable and inclusive growth (COM(2010) 2020 final) from 3.3.2010 according to which the national poverty line is defined as 60% of the median disposable income in each Member State).

"Low-income individual" or "low-income households" are often used in economic analysis and regulation. For instance the Water and Waste Services Regulation Authority recommends the provision of the access to a social tariff for low-income households.[1] But the term "low-income household" is not defined therein. Each water supplier then establishes the features of households entitled to the social tariff, mostly based on the household's income.

II. Numbers on over-indebtedness

1. How many consumers are considered "indebted" in the country?

The Portuguese Central Bank (Banco de Portugal – BdP) has provided statistics on the indebtedness of private individuals on a regular basis since 2009, when BdP released the data from the central credit register concerning this type of client (Table 1). Until then, information was provided sporadically and often mixed with other categories of clients. Because of this, we choose to deliver the data from 2009 onwards. It is worth highlighting that, according to the national statistics office (INE, 2013), in 2011, Portugal had 10,562,178 residents and 4,048,559 households. Thus, around 22.5% of residents had a mortgage, while 34% had at least one credit for consumption purposes. When we consider the total amount of credit granted to households, the data from the Bank of Portugal states that 80% of the amount is related to housing credit, while only 20% is due to consumer credit.

1 See ERSAR Recommendation n.º 01/2009, available at

http://www.ersar.pt/website/ViewContent.aspx?SubFolderPath=%5cRoot%5cContents%5cSitio%5cMenuPrincipal%5cDocumentacao%5cOutrosdocumentosIRAR&Section=MenuPrincipal&FolderPath=%5cRoot%5cContents%5cSitio%5cMenuPrincipal%5cDocumentacao&GenericContentId=0&BookID=2077

Table 1 - Number of borrowers (private individuals), by type of credit

	Housing	Consumption and other purposes
2009 Jun	2.385.655	3.737.484
2009 Dec	2.411.093	3.777.473
2010 Jun	2.440.747	3.782.192
2010 Dec	2.453.759	3.821.398
2011 Jun	2.470.738	3.801.940
2011 Dec	2.453.879	3.769.915
2012 Jun	2.424.604	3.710.341
2012 Dec	2.397.137	3.668.919
2013 Jun	2.371.783	3.615.856
2013 Dec	2.351.064	3.624.996

Source: Bank of Portugal, Statistical Bulletin, February 2014[2]

Following the 2010 Survey on Household Finance (ISFF),[3] in 2010 only 37.7% of Portuguese households (around 1,500,000 households) took part in the credit market (19.4% with mortgage credit, 11% with credit for consumption and 7.3% with both mortgage and consumption credit), against 62.3% who did not. According to the BdP's Financial Stability Report of May 2013, "household debt as a percentage of disposable income has continued to decline gradually since 2010. Nevertheless, the fact that it still remains at a very high level suggests that the adjustment process on household balance sheets will have to proceed over the next few years (Chart 1).[4]

Household debt ratio (as percentage of disposable income) has remained high. In December 2008, household debt ratio reached 122% (as a percentage of disposable income), 124% in 2009, 121% in 2010, 120% in 2011 and 118% in 2012.[5]

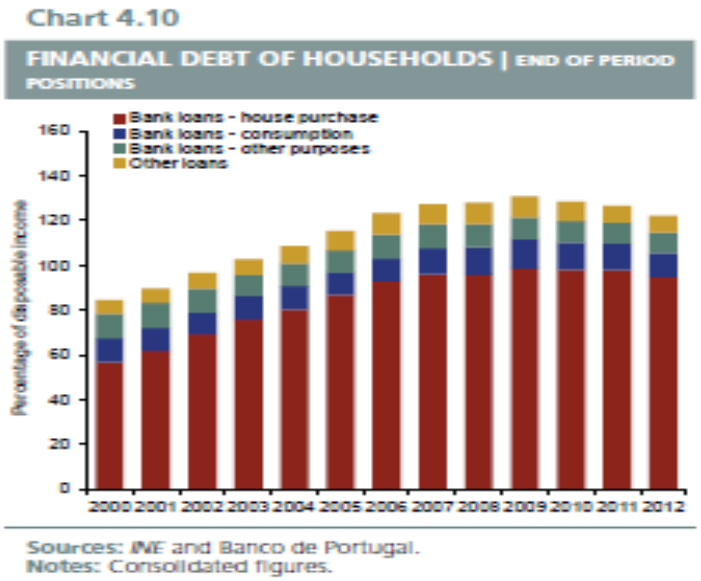
2See Bank of Portugal, online statistics (available at http://www.bportugal.pt/pt-PT/Estatisticas/PublicacoesEstatisticas/BolEstatistico/BEAnteriores/Lists/FolderDeListaComLinks/Attachments/164/BEFev14.pdf

3 ISFF is part of the Household Finance and Consumption Survey (HFCS). Its first results were released in 2012. It is conducted by the Bank of Portugal (BdP) and the National Statistics Office (INE).

4 Bank of Portugal, 2013a.

5 Households' indebtedness ratio compares the total amount of debt owed by all households to financial institutions despite credit term (5, 10, 30 years), with households disposable income of one year. That is why it can easily surpass 100%. We confront a flow variable (disposable income of one single period) with a stock variable (total amount of debt owed during several periods).

Chart 1 – Financial debt of households (% of disposable income)



Source: BdP, 2013a

Since the official statistics do not contain the socio-demographic profile of the borrower or household disaggregated by different categories of consumers, we sought additional information from financial institutions, the Association ASFAC, and the Bank of Portugal. However, this information was not made available. In some cases secrecy was cited as a reason for the refusal to disclose information.

2. How many consumers are considered "over-indebted" in the country?

The available data belongs to the main consumer defence association called DECO.[6] In 2000 DECO established the Over-indebted Supporting Offices (GAS) in its seven branches around the country. Table 2 presents the total number of files of over-indebted consumers by year.

In 2013, the number of files decreased however, according to the national coordinator of GAS, this is not due to amelioration of households' financial situation, but the opposite. GAS technicians in 2013 noticed an increase in households in a desperate financial situation that falls beyond DECO's sphere of intervention. When households face enforcement or insolvency proceedings or when they have tax debts DECO refuses to intervene. Additionally, according to the same source, even when there are no judicial proceedings going on many cases are regarded as unrecovered by means of any sort of debt repayment plan and out-of-court settlement. For those, DECO decides not to open a file. Eventually insolvency procedure is recommended.

6 There are other organizations that provide support to over-indebted households but they have fewer cases. DECO deals with more cases than all the other organizations combined.

Portuguese consumers make as much effort as possible to repay their debts even in current economic difficulties. Many households in financial distress mobilise financial support from relatives and friends to keep payments on time. That is why Portugal has a very high indebtedness ratio (129% of annual disposable income in 2012) but still has low levels of credit default (2.3% in mortgage credit and around 12% in consumer credit in 2012).

Table 2 - Number of over-indebtedness files/by year

Year	N.º of files
2000	152
2001	241
2002	379
2003	515
2004	573
2005	737
2006	905
2007	1,976
2008	2,034
2009	2,812
2010	2,837
2011	4,288
2012	5,407
2013	4,034

Source: DECO

a. How many individual consumers / households are behind with the repayment of debts?

The Portuguese Central Bank only provides information on mortgage credit and consumer credit as a whole. According to the Statistical Bulletin of the Bank of Portugal (2014), in December 2013 the number of borrowers in the household sector with overdue loans for *consumption purposes* was 601,749 (16.6% of the 3,624,996 borrowers with this type of credit in the same period) and for *housing* was 145,766 (6.2% of the 2,351,064 borrowers with this type of credit in the same period).[7] In December 2013, the percentage of borrowers in the household sector with overdue loans (housing and consumption purposes) affected 14.9% of the 4,440,899 borrowers, that is, 661,694 individuals. The Bank of Portugal considers defaults in all contracts with more than 30 days arrears. More detailed information is not available.

b. How many individual consumers / households have initiated bankruptcy proceedings?

According to statistics from the Ministry of Justice, the number of instances of insolvency of consumers or households has grown exponentially since the beginning of the economic crisis. In 2011, they exceeded even company bankruptcies (Table 3).

Table 3 - Number of bankruptcy files/by year

	2007	2008	2009	2010	2011	2012	2013*
Total bankruptcies	3909	5013	7456	9212	14680	20757	15020
Total individual bankruptcies	*732*	*992*	*1932*	*3301*	*8115*	*12632*	*9783*

Source: DGPJ – Ministry of Justice;
*until the 3rd quarter of 2013

c. How high is the average amount of outstanding debt?

7 Bank of Portugal (2014), Statistical Bulletin – March 2014, available at https://www.bportugal.pt/en-US/Estatisticas/PublicacoesEstatisticas/BolEstatistico/Pages/BoletimEstatistico.aspx.

Considering ECRI's Statistical Package Lending to Households 2012 (ECRI, 2012) we may have some figures concerning the total credit amount to households per capita, including consumer credit and mortgages.[8]

In 2000, each Portuguese citizen owed €6,750 to credit institutions, while in the awake of the crisis (2008) they owed €12,486 each. In 2011 the amount owed was €13,100 per capita, a slight decrease from 2010 when it reached €13,279 per capita.

The outstanding mortgage debt per capita in 2000 was €4,976 in 2008, €9,838 and in 2011 €10,606. On consumer credit we see that in 2000, each Portuguese individual owed €802 to credit institutions, in 2008 it reached €1,455, while in 2011 the amount owed fell to €1,406 euros per capita.

d. What percentage of those "over-indebted" consumers/households is single/married; with/without children; with/without work; retired; low-income?

According to DECO's experience, the majority of over-indebted consumers are married, with children (one or two) and employed. They belong to the middle class (medium income level) and they suffer from a previous or current unemployment situation or a decrease in salary and social benefits which has led them to their severe financial condition. In 2013, DECO professionals noticed an increase in the number of retired people and single parents.

III. Numbers on evictions

1. How many evictions have there been per year since 2000?

According to the Tenants Association of Lisbon, in 2011 there were 700,000 tenancy contracts in Portugal. Of those, only 0.2% were subject to an eviction procedure.

2. How many evictions took place because of:

a. Unpaid mortgage instalments?

In Portugal, the eviction procedure only relates to unpaid rent situations, not to unpaid mortgage instalments. For these, banks must to resort to foreclosure.

b. Unpaid monthly rent?

The number of eviction files based on rent arrears has decreased since 2003. Table 4 shows the number of evictions due to unpaid monthly rent, according to the Ministry of Justice.

Table 4 – Number of evictions, by year (2003-2011)

Year	N. of files
2003	6,873
2004	6,707
2005	6,196
2006	5,827
2007	1,778
2008	1,379
2009	1,305
2010	1,338
2011	1,399

Source: Ministry of Justice[9]

8 ECRI (European Credit Research Institute) (2012), Lending to Households Statistical Package. Brussels: ECRI

9 http://www.siej.dgpj.mj.pt/webeis/index.jsp?username=Publico&pgmWindowName=pgmWindow_635163161694218750.

These numbers must be interpreted with caution because there can be errors of classification made by the court staff. However this data seems to contradict the country's difficult economic and financial situation. One must seek explanations for this countercyclical path. Part of the explanation lies in the complexity and the slow pace of the eviction judicial procedure. In 2012, a new Rent Law (Law no. 31/2012, of 14 August 2012) simplified the eviction procedure, creating an administrative office to deal with evictions outside courts - the *Balcão Nacional do Arrendamento* (BNA), operating since January 2013. Until the end of June 2013, BNA received 1867 eviction files. From those requests, 193 were granted, 939 were rejected and the remaining are pending.

The data is scarce and cautions against making assumptions on the subject. However, we can observe an increase from 2008 onwards in the number of files for eviction. The change in the eviction procedure in 2012 aims at overcoming the slowness of courts by keeping the procedure out of the judicial system. The data of the BNA action from the first half of 2013 shows the expectations of landlords in the new procedure. However, there is no available data on the reasons for rejection for almost half of the requests.

3. Who are the persons affected?

Statistical data is missing, forcing us to provide our own perception on the matter and the perception of a lawyer, a member of a consumer association, who was interviewed.. Unemployed people may be one of the dominant groups. It is worth highlighting that there is a legal provision in the Labour Code that forbids eviction when the tenant does not pay the rent due to wage arrears (but not unemployment). As such we can admit that households affected by unemployment are more likely to be evicted.

Furthermore, young people with precarious jobs are considered a risk group, as are as the elderly. In the past, tenants older than 65 years could not practically be evicted, even when they did not pay the rents. However, this situation has changed with the new Tenancy Act which entered into force in 2013.

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage

1. Is the CCD 2008/48 implemented into national law?

Directive 2008/48/EC was transposed into national law by Decree-Law No. 133/2009 of 2 June 2009, through the mechanism of full harmonisation.

2. Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?

National law excludes mortgages over €75,000 (Art.icle2 of Law 133/2009). In practice, the majority of mortgages fall outside this legislation because of that ceiling. The general scheme of housing credit, regulated by Decree-Law n. 349/98 of 11 November 1998 is intended for households and affects loans relating to the acquisition, construction or carrying out of works in the permanent or secondary home or properties intended for lease. A household is understood as constituting of spouses or two people living in similar conditions (pursuant to Article 2020 of the Civil Code), and their immediate ancestors or descendants who also share this economic unit.

The national law on consumer credit is in line with the CCD 2008/48. However, in order to implement and standardise the application of some of the provisions introduced by Decree-Law No. 133/2009 and facilitate its supervision, BdP, which is competent under Article 17 of its Organic Law, published the following regulations.

- Notice No 10/2008, of 22 December 2008 - establishes a series of duties regarding information that are stricter and more demanding than those established for advertising in the Directive on consumer credit.
- Instruction No 8/2009, of 15 July 2009 – regulates the Standardised Information Sheet (SIS), presented in Annex I of the diploma, standardising its format and explaining its respective content;
- Instruction No 11/2009, of 13 of August 2009 – systematises the APR calculation methodology for the different types of consumer credit contracts, pursuant to the provisions in Decree-Law No 133/2009;
- Instruction No 12/2009, of 13 August 2009 – defines the categories of consumer credit with regard to the implementation of the interest rate cap regime and institutes a system of reporting consumer credit contracts concluded by credit institutions each month to the Bank of Portugal;
- Instructions No 26/2009, No 7/2010, No 15/2010, and No 19/2010 establish the maximum APR by type of consumer credit on a quarterly basis, over the period under analysis.

Optional cross-selling (bundling) is permitted and there are no legal restrictions on the type of products that can be marketed jointly. However, as conveyed by the Bank of Portugal through Circular Letter No 31/2011/DSC, of 28 April 2011, credit institutions should abstain from marketing, in association with consumer credit contracts, financial products without guaranteed capital at any time in order to improve the respective financial conditions of the parties involved.

3. *With regard to the Mortgage Credit Directive: will there have to be an adjustment of national law? What would be the changes in particular?*

The Mortgage Credit Directive (Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014) shows that some national legal provisions need to be adjusted or added, namely those referring to:

- The concept of advisory services and their standards (in Portuguese mortgage law there is no regulation of the activity of advisory services or credit intermediaries (intermediaries are only regulated in the case of consumer credit);
- Behaviour of credit institutions with regard to lending practices;
- Tying and bundling practices (Portuguese law prohibits the execution of a contract when dependent on others if there is no special connection between them, especially when it is concerns mortgage credit. In practice, however, if the consumer does not agree to add an "optional" financial product, the bank does not sign the main contract or offers less attractive conditions. In this way, facultative sales become mandatory);
- Pre-contractual information (Portugal should also reinforce pre-contractual information duties and establish a reflection period for the consumer. The "cooling off period" is not formally prescribed in mortgage regulation despite Consumer Law of 1996 enshrining such a possibility);
- Information concerning requirements and credit intermediaries' appointed representative (The Directive sets standards of conduct for intermediaries and for advisory services. These provisions only exist in Portuguese consumer credit law, and only for credit institutions and credit intermediaries);
- Assessment of the consumer's creditworthiness (Portuguese law already prescribes this duty, but some adjustment is necessary if we take into account the Proposal (number 4, article 18));
- Property evaluation;
- Approval of credit intermediaries and regulation of their activity;
- Credit intermediaries tied to only one creditor.

4. *What is the national legal framework with regard to the UCT 93/13?*

Decree-Law 446/85, of 25 October 1985 established the system of standard contractual terms. This legislation was changed to fit the Directive UCT 93/13 in 1995 and 1999 (Decree-Law 220/95, of 31 August 1995 and Decree-Law 249/99, of 7 July 1999).

Portuguese law has always been wider than Directive 93/13. While the Directive only applies to legal consumer relations, Portuguese law does not contain any such restriction, applying to the civil contracts generally. On the other hand the directive confines itself to the issue of unfair terms, not regulating issues concerning communication and clarification of contractual clauses in standard contracts as Portuguese law does. The Portuguese regime of standard contractual terms contains four parts. The first sets out the general principles, such as good faith, and the duties such as information and communication, which must be present in subscription contracts. The second and third parts of the diploma relate to clauses inserted into contracts between businesses and between businesses and consumers respectively, and regulate the clauses considered relative and absolutely banned (for being unfair). The fourth part regulates the legal instruments able to limit the application of contractual terms considered unfair.

V. Enforcement of consumer credit contracts

The legal framework which deals with household financial distress has become very complex since 2012 after the approval of many laws concerning consumer and mortgage credit default. In order to make this framework as clear as possible, we have rearranged this part of the template, distinguishing consumers in a "harsh economic situation" from those who are not.

1. Legal consequences for the loan agreement in case of default on monthly mortgage instalments. Lender's and the borrower's rights and obligations

Consumers in a harsh economic situation having a mortgage (Law 58/2012)

Law no 58/2012, of 9 November 2012, prescribes an "extraordinary procedure for households in a harsh economic situation owing a mortgage". The law defines "harsh economic situation" as a household suffering the combination of the following elements:

- At least one of the borrowers, his/her spouse or member of an unmarried couple is unemployed or the household has suffered a reduction in gross annual income equal to or higher than 35%.
- The effort rate of the household with mortgages has increased to an amount equal to or higher than 45%.
- The financial wealth of the members of the household is less than half of the gross annual income of the household.
- The real estate consists of the dwelling and a garage worth less than € 20,000.00.
- The gross annual income of the household does not exceed twelve times the maximum calculated according to the household composition and corresponding to the sum of the following items:
- For the debtor: 100% of the national minimum wage (equal to €485 per month) or 120% of the household is composed only by the applicant. For each of the other adult members of the household (over eighteen years old): 70% of the national minimum wage. For each household member that is a minor (under 18 years old): 50% of the national minimum wage (NMW is currently €485 per month). The property in question has been subject of a loan agreement with mortgage. The taxable value of the property does not exceed specific legal limits.

The mortgage loan is not secured by other real or personal guarantees. In the latter case, if the guarantors are also in very difficult economic situation, as per the terms already mentioned, the regime is applicable.

In case of default of a debtor in a harsh economic situation, under Law No. 58/2012, the credit institution is obligated to present a plan for restructuring the mortgage loan and additional measures, if necessary (e.g. credit consolidation).

According to Law No 58/2012, the restructuring plan may consist of:

- Granting grace periods on payment of monthly instalments over the borrower or the establishment of a residual value it the amortisation schedule - within twelve (minimum) to 48 (maximum) months.
- Extending the amortisation period of the loan - up to 50 years in relation to the date of the credit contract.
- Reducing the applicable spread during the grace period - minimum of 0.25%
- Granting an additional loan, intended to temporarily support the payment of the mortgage loan
- Credit consolidation
- If the *plan is not viable*, or if the debtor refuses it, the debtor is entitled to *substitutive measures* that prevent foreclosure namely:
- Transfer of the property to the bank in lieu of payment.
- Sale of the property to a FIIAH (Real Estate Investment Fund for Rental Housing), promoted and agreed by the credit institution.
- Exchange for a less expensive house, followed by a review of the credit contract that includes a capital reduction (by the amount of the difference between the values of the two dwellings).

Lender Obligations/ Borrowers rights:

- The credit institution is forbidden to initiate judicial proceedings against the debtor, including foreclosure.
- The credit institution is legally obligated to submit a proposal for a restructuring plan to the borrower;
- The debtor's request to benefit from this procedure, submitted to the creditor, automatically suspends foreclosure and other procedures connected to the mortgage loan;
- The credit institution must inform the court of this request if there are judicial proceedings.
- In all of their contracts, the credit institution must provide the debtor with simple and clear information about the procedure and the debtor's rights.

Borrowers Obligations / Lenders Rights

The borrower must fulfil certain legal requirements in order to access this procedure. These requirements are what put the borrower in a harsh economic situation. The borrower cannot lie about those requirements, and if they do so they must compensate the credit institution for its losses.

Consumers not in a "harsh economic situation" having a mortgage or with consumer credit (Law 59/2012 and Decree-Law 227/2012

For a consumer with a mortgage but not in a harsh economic situation there are two complementary regulations: Law 59/2012 (that amended Decree-Law 349/98 11 November) and Decree-Law 227/2012. When default is associated with a credit other that mortgage credit, debtors benefit from the regime of the aforementioned Decree-Law no. 227/2012.[10]

Law 59/2012 of 9 November 2012, creates some additional safeguards for borrowers with regards to housing loans. In case of default of a consumer not in a harsh economic situation, credit institutions

10 The new regime of 2012 must also be combined with that of Decree-Law 133/2009 of 2 June 2009, that transposed the CCD 2008/48.

may only execute the resolution or any other form of cessation of the contract after three overdue payments of the debtor.

Lender Obligations/ Borrowers rights:

- Credit institutions cannot aggravate the credit terms, including increasing spreads, in case of renegotiation of the contract in the light of this legal regime
- The credit institution must inform the debtor, in simple and clear language, about the applicable rules in case of a contract failure.
- The credit institution must inform the consumer about the existence of special measures, namely, the transfer of the property in lieu of payment and its judicial selling, which may, under certain conditions, exonerate the debtor from the entire payment of the credit.

Borrowers Obligations / Lenders Rights

Law 59/2012 does not stipulate any obligations to the borrowers. However, the general rules of contract law may be applicable, namely the fulfilment of the good faith principle.

Decree-Law 227/2012 establishes the principles and rules to be complied with by credit institutions to prevent and settle cases of default in loan agreements (consumer credit and mortgage credit excluded from the extraordinary procedure of Law 58/2012) signed with bank customers. This Decree-Law is applicable to debtors with consumer credit and also with mortgage credit if the debtor *is not in a harsh economic situation,* and establishes the principles and rules to be observed by credit institutions in case of default, among other things.[11] The credit institution is forced to initiate an extrajudicial settlement with the debtor (PERSI) between the 31st and the 60th day of arrears.

Lenders Obligations / Borrowers Rights

There is a general obligation for lenders to act in a loyal and diligent manner and to adopt the necessary measures to prevent credit default and to rectify the situations of default (Article 4 (1)). Credit institutions shall promote the necessary steps, in order to implement an out-of-court procedure (PERSI), regarding debtors who are in arrears.

Borrowers Obligations / Lender Rights

Consumers should manage their obligations related to responsible credit according to the principle of good faith, timely alerting the credit institutions to the eventual risk of default of obligations under credit agreements and collaborate with them in finding solutions for the extrajudicial compliance with these obligations (Article 4 (2)).

2. Requirements to initiate enforcement procedures against the consumer

Consumers in a harsh economic situation having a mortgage (Law 58/2012)

If a borrower in a *harsh economic situation* has not fulfilled the restructuring plan and has not requested substitutive measures of foreclosure, the credit institution can apply to the judicial courts for seizure.

Consumers not in a harsh economic situation having a mortgage or with consumer credit (Law 59/2012 and Decree-Law 227/2012)

11 Besides out-of-court settlement of credit default, this law prescribes two more regimes: that each credit institution has to create its own Action Plan for Risk of Failure (PARI) to monitor its clients and prevent their default; that each credit institution must inform the debtor in arrears of the existence of the out-of-court network that can provide support to debtor in arrears (network RACE). RACE network came into force in mid-2013. It includes twelve organisations mostly of civil society recognised by the General Directorate of Consumers Affaires and the Bank of Portugal. The fact that the law forbids them to contact directly the financial institutions to renegotiate on behalf of the consumer has been seen as a step back in the previous experiences of debt counselling such that of DECO (who do not belong to RACE).

In the light of the regime of Law 59/2012, if a borrower fails to pay three overdue instalments, the credit institution can apply to the courts through an enforcement action and the creditor can seize assets of the debtor. Following the regime established in Decree-Law 227/2012, PERSI is initiated when one of the following situations occurs (Article 14):

- − immediately after the situation of being "in arrears" and the customer's request to the bank;
- − Between the 31st and 60th days after the breach;
- − Once the customer, after the bank's warning of the risk of entering into default, delays any instalment

3. What are the steps for such an enforcement procedure?

Consumers in a harsh economic situation having a mortgage (Law 58/2012)

According to the regime of Law 59/2012, the credit institution will interpose an enforcement action against the debtor in court (the credit contract is a title for immediate enforcement action). After that the debtor is notified to contest the seizure. Finally the judge decides on the enforcement action.

Consumers not in a harsh economic situation having a mortgage or with consumer credit (Law 59/2012 and Decree-Law 227/2012)

In the light of the regime of *Law 59/2012,* the credit institution will impose an enforcement action against the debtor in court (the credit contract is a title for immediate enforcement action). After that the debtor is notified to contest the seizure. Finally the judge decides on the enforcement action.

Following the regime of Decree-Law 227/2012, when a debtor falls under one of the three situations foreseen in Article 14 the bank must integrate the debtor into the PERSI regime and within five days should notify the debtor of that fact. Then follows an evaluation phase that cannot surpass 30 days during which the creditor ascertains if debtor's situation is transitory or not. Within ten days the debtor has to provide all the documents and information requested by the bank so it can make an accurate analysis of the financial situation of the client (Article 15 (1) – (3)). After that 30 day period the bank informs the client: i) that the evaluation shows no possibility of debt recovery (other than the general legal hypothesis of judicial debt collection); or ii) the proposal for debt recovery, including, for instance, the renegotiation of the contract terms or credit consolidation (Article 15 (4)). The next phase is the renegotiation of the proposal presented by the bank to the debtor, where the debtor can make a counterproposal or even refuse the initial proposal (Article 16). The PERSI is extinguished when (Article 17 (1)):

- full payment of the amount due by the debtor is made;
- the parties reach an agreement;
- on the ninety-first day from the beginning of the PERSI;
- with the bankruptcy of the debtor.

When the creditor and the debtor do not reach an agreement, the debtor may, within five days, request the intervention of the Credit Mediator (Article 20). The Credit Mediator is an independent office located at the Bank of Portugal that can receive complaints from bank clients relating to credit refusal or credit arrears (Decree-Law 144/2009, of 17 June 2009). The Credit Mediator can act in such cases as a debt advisory service by helping the parties to come to an agreement. During its intervention, the debtor benefits from all the guaranties provided by the Decree-Law 227/2012 (see below).

The consumer can also raise objections against enforcement. These objections differ depending on whether the consumer is in a "harsh economic situation" or not.

Consumers in a harsh economic situation having a mortgage (Law 58/2012)

After the enforcement procedure is initiated the debtor can raise substantive objections based on the absence or unenforceability of the title, lack of any mandatory procedure requirements, missing or invalid notification of the debtor, uncertainty or unenforceability of the obligation, the existence of a fact that can extinguish the obligation, or the prescription of the right or obligation. The judge must decide if the objections evoked are admissible and if they may or may not extinguish the creditor's request.

Consumers not in a harsh economic situation having a mortgage or with consumer credit (Law 59/2012 and Decree-Law 227/2012)

In the light of the regime of *Law 59/2012*, after the enforcement procedure is initiated, the debtor can raise substantive objections based on the absence or unenforceability of the title the lack of any mandatory procedure requirements, missing or invalid notification of the debtor, uncertainty or unenforceability of the obligation, the existence of a fact that can extinguish the obligation, or the prescription of the right or obligation. The judge must decide if the objections evoked are admissible and if they may or may not extinguish the creditor's request.

According to *Decree-Law 227/2012*, related to default in consumer credit and mortgage credit not in a harsh economic situation, the credit institutions are forbidden to charge commission when they renegotiate the contract conditions subject to PERSI. Furthermore, during this procedure the credit institutions cannot (Article 18):

- Solve the credit agreement through the contractual default mechanisms;
- Initiate legal proceedings in order to satisfy their credit;
- Transfer part or the entire claim to a third party;
- Transfer their contractual positions to a third party.

4. Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?

Contrary to the Brazilian legislation and jurisprudence that welcomes the theory of unforeseeability regarding consumer protection law, Portuguese legal thought and jurisprudence have never been very fond of this approach.[12] Not surprisingly this approach has not been applied to default of credit contracts as such (not even when default is caused by unemployment or illness). The discussion of the *rebus sic stantibus* principle includes several different issues such as the "delimitation between the error in the basis of the transaction ("erro sobre a base do negócio") and the regulation for the alteration of circumstances",[13] the concept of unforeseeability, the abnormality of the change, the protection of legitimate expectations, etc.[14]

However, recent jurisprudence has begun to show some signs of "sensitivity" to current economic conditions and their effect on the performance of the contracts. At least in the case of companies there are already a number of judicial decisions on interest rate swaps in which the courts have come to decide the termination or modification of the contract based on the abnormal change of the circumstances in which they were signed.[15] The courts have held that the large and protracted decline in interest rates caused by the financial crisis has created a serious imbalance in the contractual

12 See Ascensão, José de Oliveira (2004), Alteração das circunstâncias e justiça contratual no novo código civil , available at:

http://www2.cjf.jus.br/ojs2/index.php/revcej/article/viewFile/605/785; Fernandes, Luís Carvalho (2001) A Teoria da Imprevisão no Direito Civil Português - Reimpressão com nota de actualização, Coimbra: Almedina.

13 Monteiro and Gomes, 2006.

14 Fernandes, Luís Carvalho (2001), A Teoria da Imprevisão no Direito Civil Português - Reimpressão com nota de actualização, Coimbra: Quid Iuris.

15 See the Judgment of the Appeal Court of Porto of 14th July 2012.

obligations, compared to what the parties had represented as possible and wanted to ensure through those swap contracts.

The understanding that is being used by Portuguese courts for certain credit agreements concluded by the banks with small businesses (and that are therefore not included in the legal regime of consumer credit laid down in Decree-Law 133/2009 of 2 June, which transposed Directive 2008/48/EC), could and should, in our view, be extended to consumers and households. This would help to create a new balance between the dominant principle of *pacta sunt servanda* and the principle of *rebus sic stantibus*, or, in other words, would balance the risk of default in new ways.

a. How is the term "unforeseen/unforeseeable events" defined?

In Portuguese contract law, if the foundations of the contract suffer a fundamental change it is possible, according to the Portuguese civil code, to ask for an adjustment or, alternatively, for the rescission of the contract. This is due to *unexpected change of circumstances* ("alteração anormal das circunstâncias") prescribed by Article 437º of 1966 Civil Code.

According to the Portuguese doctrine the concept of the unexpected is broader than that of the unforeseeable (Monteiro and Gomes, 2006; COSTA, 2001)[16]. Article 437/1, states that "if the circumstances in which the parties based their decision to contract change unexpectedly, the injured party has the right to terminate the contract, or to alter it according to fair judgement, as long as the requirement of the obligations which it assumed seriously affects the principles of good faith and is not covered by the actual risks inherent in the contract".

The right of one of the parties to terminate or modify the contract "according to fair judgement" only exists "as long as the requirement of the obligations which it assumed seriously affects the principles of good faith and is not covered by the actual risks inherent in the contract".[17] Some authors like Ascensão (2005) state that "the possibility of asking for a modification of the contract, under article 437, is not restricted to cases where one or both of the contractual partners suffer losses as a result of supervening events. It may also occur whenever the economic balance of the contract is seriously compromised by unforeseeable circumstances." [18]

Portuguese jurisprudence has understood that the unexpected alteration of circumstances must cause an imbalance in fulfilment, making performance of the contract excessively onerous or difficult for one of the parties.[19] This has been seen as a "distant cousin" of the *rebus sic stantibus* principle and the theory of unforeseeability.[20]

b. If adjustment is possible, what are its legal effects?

Adjustment is one of possibilities prescribed by Article 437º of Civil Code. In such cases the modification of the contract is made according to equity.

16 Costa, Mário Júlio de Almeida (2001), Direito das Obrigações, 9th ed. Coimbra: Almedina.

17 See the Judgement of the Supreme Court of Justice of January 18th, 1996.

18 Ascensão, José de Oliveira (2005), Onerosidade Excessiva por Alteração das Circunstâncias, ROA, 65; Monteiro, António Pinto and Gomes, Júlio (2006), Hard Core Cases on Unexpected Circumstances, available at http://www.unexpected-circumstances.org/.

19 See the Judgement of the Supreme Court of Justice of September 30th, 2004.

20 Usually, unforeseeable events may be due to fortuity or to force majeure. Fortuity is the development of natural forces that remain outside someone's control (flood, fire, ...). Force majeure is an external factor, for which the debtor cannot be liable (war, imprisonment, theft, ...). The concept of force majeure is underlined by the idea of inevitability. Some authors consider 'fortuitous event' and 'force majeure' to be synonymous, indicating that both concepts report to an event which creates an inability to comply or which is not attributable to the will of the debtor or the creditor. See Neto, José Lourenço (2006), Imprevisão: uma teoria prática na socialização dos contratos, avalilable at http://www.boletimjuridico.com.br/doutrina/texto.asp?id=1374.

5. Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?

According to Baptista Machado (in Monteiro and Gomes, 2006), one must differentiate between "certain obligations, which are neutral in terms of purpose (which is typically the case in sale and purchase obligations), and others in which, due to the actual type of contract or to the agreement between the parties, the provider accepts the possibility of a connection between the rendering of his service and a determined purpose or aim of the recipient by which the rendering of this service becomes impossible from the moment that the intended purpose is not able to be achieved".

If the purpose of the contract was frustrated by circumstances not attributable to either party, the provider is entitled only *to be compensated for the work and expenses that he has already carried out*. Following Monteiro and Gomes (2006), *frustration of the purpose* of rendering the contractual goods or services "is not expressly provided for in law. The loophole would be filled, by analogy, by means of Article 468, n˚1, of the Civil Code on transactional management, or preferably by means of Article 1227 of the Civil Code on the impossibility of carrying out the work in the building contract." This approach has not been applied to default of credit contracts as such.

VI. National legal framework applicable for over-indebtedness

1. What are the possibilities for consumers in case they are considered "over-indebted"?

a. Is there the possibility for the consumer to reorganise debt or obtain debt relief?

In Portugal a consumer can obtain re-organisation of the debt or debt relief by initiating an insolvency procedure, an out-of-court procedure (PERSI) or when they are in a harsh economic situation (Law nº 58/2012). These last two procedures are described above. The insolvency regime is the only one that is truly related to over-indebtedness and that provides debt relief, although under very strict conditions.

i. How are the terms re-organisation and debt relief defined?

Re-organisation is not defined by law. The Decree Law 227/2012 only prescribes examples of re-organisation measures, like credit consolidation and the rearrangement of contract terms (art. 15/4 *b)* of Decree-Law 227/2012 concerning the PERSI regime).

ii. What are the requirements for re-organization and relief?

See the above description of PERSI's regime under issue *V Enforcement of consumer credit contracts*.

iii. How many consumers have had debt reorganised

No available data.

iv. How many consumers have obtained debt relief?

No available data.

b. What are the requirements for initiating bankruptcy proceedings for consumers?

According to the Bankruptcy Code (CIRE), the consumer is considered insolvent when he/she is unable to fulfil its due obligations (article 3).

Therefore, the first requirement to be fulfilled by the debtor is to be insolvent or in a situation of imminent insolvency. In addition, the petition for insolvency should contain the following elements:

- Indication of insolvency or imminent insolvency
- Request for discharge of debt (initial request for discharge)
- Identity of the five main lenders

- Identity of the spouse if married and marital property regime
- Certificate of the civil registry and, eventually, the commercial register in case of a small entrepreneur.

c. Is there a possibility for consumers to attain discharge of debt within bankruptcy proceedings?

Yes, under the discharge mechanism prescribed by the Insolvency and Corporate Recovery Code (CIRE) of 2004 (Bankruptcy Code). According to jurisprudence, "the dismissal of the remaining liability is a mechanism whose ultimate goal is the extinction of the debts of an individual and the release of part of his liability in a shorter and lighter way than traditional prescription, corresponding to the objectives of the legislator to grant the debtor a second chance and to provide priority to his rehabilitation."

i. How is discharge defined in the national context? (Is there a definition?)

CIRE 2004 refers to debt relief - *exoneração do passivo restante* – as the dismissal of the claims on the insolvency that are not fully paid during the insolvency proceedings, or five years after the termination of this procedure (Article 235 of CIRE).

ii. If discharge is possible, after how many months/years is it possible?

According to the Article 231 of CIRE, discharge can be granted five years after the termination of bankruptcy procedure (this term starts right after the closure of the liquidation of non-exempt property).

iii. If discharge is possible, what are the requirements for discharge?

When filing for bankruptcy the debtor must provide a request for discharge (initial requirement of discharge). Subsequently the judge analyses this request and approves or denies it.

If the judge approves this initial request, the bankruptcy procedure continues on its regular path: liquidation followed by five years of probation (the so-called assignment period). In the end, the judge evaluates the debtor's behaviour during the procedure and during the assignment period, considers creditors' opinions and decided whether or not to grant the discharge of the remaining debts. The judge must establish an amount fo household living expenses that cannot exceed (except in very limited circumstances appreciated by the judge such, for instance a huge number of dependents or a particular medical condition) the equivalent to three national minimum wages (that is, three times €485) per month.

- If the initial request is denied, the procedure will end with a sale of assets. After this, creditors can seize the debtor's remaining debts until their prescription (in some cases, prescription lasts for 20 years).
- Discharge can be granted if the debtor:
- Presents a timely request for discharge
- Does not present a payment plan
- Has not obtained credit or subsidies in the three previous years, using false or incomplete information
- Has not received discharge in the last ten years
- Files for bankruptcy in the six months after the insolvency arise
- Does not provide elements, at the time of decision, that suggest in all probability the existence of fault of the debtor in the creation or exacerbation of insolvency for the purposes of the bankruptcy
- Has not been convicted by wilful criminal insolvency in the last ten years

- Has not violated duties of information, presentation and collaboration during the insolvency procedure, by intent or gross negligence
- Has made all the efforts to keep or to find a job

iv. How many consumers have obtained debt discharge?

We cannot provide reliable information since a careful analysis of the database of the Ministry of Justice (website *CITIUS*) shows that court staff record the proceedings incorrectly in the database. They record as final decisions of debt discharge the initial orders of admission of debtor's application for discharge. Given the duration of the proceedings (at least six years) we estimate that only a handful of cases reached the end of the five year probation period established in the Bankruptcy Code.

d. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

Although there is no official information, according to some judges the procedure lasts around seven years. After being declared bankrupt, the debtor will see their property sold by a trustee appointed by the court. This operation can take some time, especially in the current economic crisis. After the conclusion of the sale, a probation period of five years starts during which the debtor must surrender to the court their remaining income to allow the repayment of the creditors. Only then, and after the court confirms their "good behaviour", will the debtor be entitled to discharge of debt.

e. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can have recourse to?

Many consumers use the existing normal ADR procedures, including the over-indebted supporting offices (GAS) created by the consumer association DECO.

However there are now new alternative means of resolving disputes that enable regularization of credit defaults directly with the financial institutions outside the courts (the PERSI regime).

2. Is there a national legal or policy framework for avoiding evictions?

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (i.e. debt relief)?

The current policies seem to aim at accelerating evictions. The new administrative office - the *Balcão Nacional do Arrendamento* (BNA) – is part of an attempt to overcome the inability of courts to solve such actions in due time. The only measures that allow consumers to remain in their homes during the insolvency proceedings are:

- Submitting a payment plan to creditors to avoid asset liquidation
- Through the new Special Procedure of Revitalisation (although this procedure mainly suits business and has never been used by private individuals except in a handful of cases mostly related to self-employed individuals)
- Substitutive measure to prevent seizure - this measure consists of the sale of housing to a Real Estate Investment Fund for Rental Housing (FIIAH). The amount paid by the Fund is directly delivered to the credit institution. The sale of the property to a FIIAH only extinguishes the entire debt if the sum of the amount paid by the FIIAH to purchase the property and the sums paid by bank customer as repayment of capital is at least equal to the loan amount, or if the amount paid by the FIIAH for the acquisition of the property is lower than the capital in debt.

When the sale of the property to FIIAH does not extinguish the entire debt, the consumer remains liable for the payment of the amount equivalent to the difference between the outstanding amount and the property sale's value.

The consumer cannot refuse to sell the property to a FIIAH if the creditor chooses this measure, under the penalty of losing the right to apply to another protection measure. However, it should be noted that this measure can only be applied if the consumer proves to be in a *harsh economic situation* and, although the law does not explicitly state this, they are not able to apply for the insolvency procedure.

b. Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

Theoretically, banks that receive the houses in any situation can rent it to the previous owner. However, as far as we know this measure as not been put into practice.

VII. The regulation of credit bureaus

1. How many credit bureaus are there in the country?

There are two credit bureaus.

2. Are the credit bureaus public or private?

One credit bureau is public – *Central de Responsabilidades de Crédito* (prescribed by the Decree-Law 204/2008, of 10 October 2008) – and managed by the Bank of Portugal. The other is private – Credinformações – and belongs to Equifax. These are competing credit bureaus, although the public database covers more institutions, including major banks, than the second one. In turn, the private database is updated more regularly than the second (this one is only updated monthly).

3. How are credit bureaus compensated?

The public credit bureau is part of the supervision obligations of the Portuguese Central Bank, who bear its costs. However, financial institutions that query the database pay a fee for each consultation. This fee can be passed on to the client. For the Credinformações the payment is negotiated with each participant. The terms are not disclosed.

4. How do the credit bureaus collect data?

The data of the credit bureaus come from financial institutions (secrecy regime) registered in the database. In the case of the public credit bureau, all financial institutions subject to Bank of Portugal's supervision are obligated to provide information to the database every month about credit contracts above €50. Regarding Credinformações, only the institutions that voluntarily subscribe to this database provide the information.

In both cases, the participants in the credit bureau provide information about credit contracts and their fulfilment (positive data), as well as payment incidents in any contract (negative information).

The Bank of Portugal database probably collects more positive information than Credinformações, because this private credit bureau, unlike the public one, is subject to banking secrecy. Because of that, the five main banks do not work with the Credinformações credit bureau.

5. In what way do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

Article 17 of the Law 67/98 (Data Protection Law) of 26 October 1998 prescribes the duty of secrecy to every person or organisation that deals with personal data. This includes credit bureaus. This duty is also prescribed by the legal regime of financial institutions, including supervision entities (Article 80 of Decree-Law 298/92).

6. What data is collected by credit bureaus?

Since both credit bureaus possess positive and negative files, they collect data related to credit contracts celebrated by financial institutions and their clients. This includes the contracted amount, duration and regular payment (positive information), as well as payment incidents (negative information).

In the case of the Bank of Portugal's database, the information collected includes:

- Identity of the customer and the amount of their credit liabilities, classified according a set of features such as the level of responsibility, financial product type, the original period, the residual maturity, the credit crunch, the class of non-performing loans (where applicable), the currency of the credit
- Information about type and amount of collateral and monthly instalments.
- Declarations of bankruptcy.

7. Who are the users of credit bureaus?

According to the reciprocity principle, the data providers are those who can access credit bureaus' information. Every month, the BdP database releases to the providers the total number of financial responsibilities undertaken by each of their clients. If a bank receives a credit request from a new client, the bank can require the client's authorisation to access their profile in the BdP database.

(Over-)indebtedness of consumers

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country?

The report "*A actualidade do sector imobiliário residencial*: *ajustamentos e desafios*", of November 2011 of the main Portuguese commercial bank (public) called Caixa Geral de Depósitos (CGD) analysed the Portuguese housing market and concluded that there was no "housing bubble" in the country.

"Between 1996 and 2006, the cumulative appreciation of real house prices exceeded 80% in the U.S., the Netherlands and Greece, 90% in France, 110% in Spain, 140% in the UK and 180% in Ireland. These figures contrast with the rise of less than 10% in Portugal and the trend of long-term devaluation in Germany, only interrupted in 2008. Only in the years before the subprime crisis (2003-2006), the cumulative appreciation of the nominal housing prices went up 50% in Spain and France, 40% in the U.S., UK and Ireland and 30% in Greece in contrast to 5% in Portugal and the -1% decrease in Germany" (CGD, 2011).

According to the European Mortgage Federation, in 2009 Portugal had an owner occupation rate of 74.6% (the EU average was 68.9%). Only 30% of the population had a mortgage, while 44.6% had no burden of housing, 11% had rented housing and 14.4% paid social rent (CGD, 2011)

2. What is the relation between housing prices and over-indebtedness?

a. How have housing prices developed since 2000?

In its 2010 Annual Activity Report, the Bank of Portugal stated that:

> "house prices in the period 1997 to 2006 increased at a high rate in Ireland, Spain, France, Greece and the Netherlands (between 6.0 per cent and 10.9 per cent) and more moderately in Italy (2.8 per cent) and Portugal (0.7 per cent). On the contrary, real prices in Germany decreased by an average of around 1.5 per cent." (BdP, 2011).

The Portuguese Central Bank refers to International Monetary Fund (IMF) that claims that:

> "the house price gap in 2007 was between 20 and 30 per cent in Ireland and the United Kingdom, between 10 and 20 per cent in France, Spain, Italy and the Netherlands and around 7 per cent in the United States. The deviation in Portugal was close to zero, and in Germany around -5 per cent."(BdP, 2011).

In Portugal, the drop in house prices started with the financial crisis and is mostly due to the decrease on the demand side, an initial increase in interest rates and more restrictive criteria on the credit supply side.

Furthermore, the Global Property Guide[21] confirms that:

"the house price boom that swept through most of Europe and the developed world from the mid-1990s to 2006 missed Portugal. Except in 2003, house price growth in Portugal has been generally lackluster.

2003 - 2004, house prices rose by an average of 6.2% y-o-y (3.3% in real terms);

2005 - 2007, prices rose by an average of 1.25% (-1.3% in real terms);

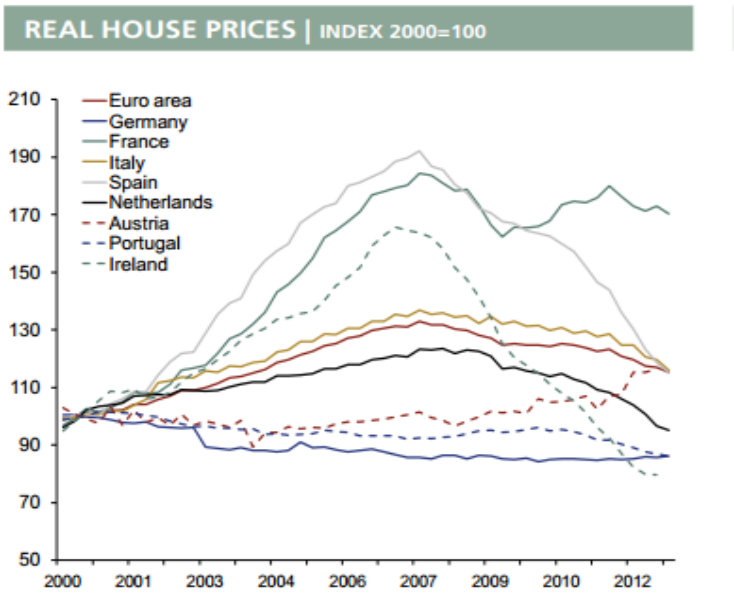
2008 - prices fell by an average of 4.7% (-7.1% in real terms);

2009 -prices fell by an average of 2.6% (-1.8% in real terms);

2010 - 2012, house prices fell by an average of 3.1% (-5.5% in real terms)".

The Bank of Portugal's 2012 Annual Report –The Portuguese Economy (BdP, 2013b) shows the evolution of house prices in Portugal, the Eurozone and other EU countries, since 2000 (Chart 2)[22]. The data are in line with those of the Global Property Guide.

Chart 2 – Real House Prices



Source: BdP, Eurostat and ECB

b. How has the number of over-indebted consumers developed since 2000?

21 http://www.globalpropertyguide.com/Europe/Portugal/Price-History.

22 Bank of Portugal (2013b), 2012 Annual Report –The Portuguese Economy, available at https://www.bportugal.pt/en-US/EstudosEconomicos/Publicacoes/RelatorioAnual/Publications/RA_12_e.pdf.

According to DECO, the main consumer defence association, the total number of files of over-indebted consumers, per year, increased significantly since 2000, but 2007 and 2011 showed the most significant changes (Table 5).

Table 5 - N. of over-indebtedness files/by year

Year	N.º of files
2000	152
2001	241
2002	379
2003	515
2004	573
2005	737
2006	905
2007	1,976
2008	2,034
2009	2,812
2010	2,837
2011	4,288
2012	5,407
2013	4,034

Source: DECO

These numbers are certainly not complete; they only give us an indication of the overall development of over-indebtedness in Portugal. This is because the DECO data is limited by the scope of DECO services. DECO only provides support to consumers whose debts fulfil certain criteria: the individuals (consumers) must have acted in good faith[23] and they must show a clear inability to cope with all of its non-professional debts. These debts cannot result from the exercise of their professional activity. Tax debts and the debts that have generated lawsuits are also excluded from DECO's intervention.

This means that DECO receives more support requests than the number of files it opens. According to the interview conducted with a DECO representative in 2013 the association only opened a few more than 4,000 files, but received around 29,000 requests. This means that, according to the same source, a significant part of the consumers do not fulfil the established criteria for DECO intervention, mostly because they have professional debts as well (small traders) or because they are already subject to enforcement proceedings required by some other creditor. Another important group of rejected consumers are those who are regarded as incapable to accomplishing any renegotiated plan due to their extremely dramatic financial situation. For these cases, insolvency is often recommended. Thus, taking together these numbers with the insolvency numbers would probably provide a picture closer to the real numbers.

3. *Has there been increased access to mortgage credit? In which way? And has access to credit become more restricted since the crisis?*

In Portugal, the development of consumer credit market took place later than in most EU member states. From the nineties, changes from the point of view of both supply and demand converged in a favourable social and economic climate. It was then that credit for consumption and housing dramatically grew turning different social classes and strata into debtors.

23 The good faith principle, established in contract law prescribes the duty of the creditor and the debtor to act with propriety and honesty, with loyalty and integrity.

In the late seventies and eighties the expansion of consumer credit was severely restricted. The progressive liberalisation and deregulation of the Portuguese financial system, in particular the banking sector, was driven by the introduction of the Single Market for Financial Services. It was only in the beginning of the nineties that the right conditions were created for the strong growth (in real terms) of consumers' credit.

The same strong growth was seen in housing credit, which represents the main source of consumer indebtedness (around 80% of total consumer debt). At the beginning of the nineties, the use of bank credit for housing was still substantially below the European average. But after that it has rapidly approached the average patterns of indebtedness in the European Union and has registered some of the highest growth rates in Europe for housing credit. More than 50%of consumer credit used to be referred to car loans, while credit cards did not have a significant impact in households indebtedness, at least in the pre-crisis period. In 1999, the rate of consumers' indebtedness represented 76.5% of their disposable income while in 1990 it only reached19.5%. In 2008 it increased to 132%.

One of the immediate effects of the crisis on the financial markets was a decrease in credit available to businesses and families. In the case of households, the housing loans became almost impossible to obtain and the applied spreads increased significantly. The Retail Banking Markets Monitoring Report published for the first time this year by the Bank of Portugal states that:

"in 2012, the consumer credit market shrank sharply, even more so than in 2011. The reduction in the number of contracts concluded and the amount of credit provided was very significant and was accompanied by a fall in the average amount provided. The contraction affected all credit types and was accompanied by a rising in the average APRC, which inverted its trend from the fourth quarter of the year."

Before, in 2003, 12,944 million euros were granted in housing loans. In 2004, credit reached € 18,260 million and in 2007 it achieved the highest value of the decade between 2003 and 2013, with €19,630 million. But after that year, the fall was abrupt, decreasing to 13,375 million in 2008 and to € 1,935 million in 2012. From 2013 onwards, there is an improvement in the offer and demand of housing loans, but the available data refers only to the first nine months of the year. Until that time, € 1,469 million were granted in housing loans, a value slightly greater than that of the same period in 2012 (APEMI, 2013)[24].

This reality is also reflected in the spreads charged by major banks. In 2011 and 2012 the spreads maintained at the higher values of the last two decades, with the minimum spreads at 4.5%. After the second half of 2013, some banks lowered these spreads to around 3%. However, according to the Bank Lending Survey of January 2014, the five largest banks operating in the national market continue to state that they intend to continue to maintain the same restrictive criteria for granting housing and consumer loans that they have been applying in the last two to three years.

It was not just the amount of credit and the price that worsened in recent years. The percentages of financing and warranties have also become more demanding. If, prior to the crisis, it was possible to obtain financing for 100% of the property value, this is no longer possible. Banks began to finance the full value of the property only in the case of immovable property purchased by the banks themselves and those reacquired following judicial collection proceedings, insolvencies or transfers in lieu of payment.

With regard to guarantees, there has been an increase in the requests for guarantors and insurances from the banking sector, according to the information provided by a bank employee who agreed to be interviewed.

4. What is the relation between employment and over-indebtedness?

24 APEMIP (2013), Catálogo de Estudos de Mercado, 23, 4th quarter of 2013.

a. What percentage of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when over-indebtedness arose?

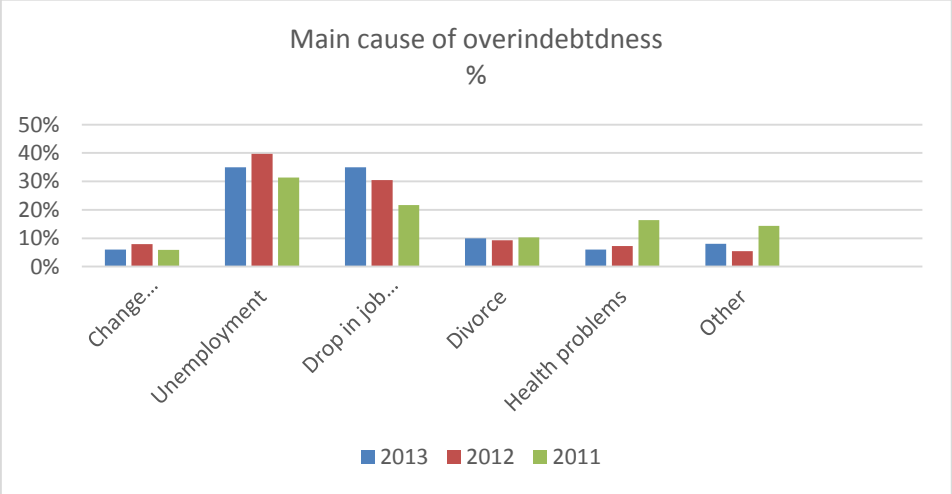
Unemployment and deterioration in job conditions have been, for a long time, the main causes for Portuguese households' over-indebtedness (Frade *et al*., 2006).[25]

According to DECO's statistics, from 2011 until 2013, unemployment of one or two members of the couple is the leading cause for financial hardship (on average, 89% of unemployment cases consisted of the unemployment of one of the household's adult members, while in 11% both adults were unemployed), followed by the worsening of job conditions (e.g. salary reduction, delay in salary payment, cut in overtime hours or productivity benefits, part-time job). These two factors combined are responsible for around 70% of DECO's cases. Divorce and health problems come next on the list, but with a much smaller impact (Chart 3).

Although unemployment is the main cause for debt default, most of the consumers seeking DECO's assistance in renegotiating their debts with the creditors, were employed again at the time of the renegotiation.

According to DECO's representative, in 2013, 70% of the files were related to unemployment and to salary and retirement benefits cuts. DECO also points out an increase in single persons (with or without children) files, even though married people are still the majority of the cases.

Chart 3 – Main cause of over-indebtedness in DECO's files



Source: DECO

b. How has the average salary evolved since 2000?

By 2011, nominal wages were generally increasing. However, when observing their real value, in comparison to 1995, it appears that since 2000 the value of wages has remained relatively stable until 2011, when it began to decline gradually (Table 6).

Since 2000, public servants' salaries remained practically unchanged for the medium and high level careers, except in 2009 (an election year) when there was a (modest) rise in salaries. In 2010, the Portuguese government announced the first salary cuts to be implemented from 2011 onwards. Since then, other wage cuts were applied to them.

25 See Frade, Catarina et al. (2006), Desemprego e sobreendividamento: contornos de uma ligação perigosa, Coimbra: CES.

Table 6 - Real compensation of employees (1995=100)

Year/Real compensation of employees (1995=100)	1995	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
	100	*103*	*101*	*100*	*101*	*100*	*102*	*99*	*101*	*101*	*102*	*101*	*99*	*97*

Source: Eurostat

5. Non-EURO countries

6. Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?

The worsening conditions of the job market are part of the problem of the current financial difficulties faced by Portuguese families. The country has been under international financial supervision since May 2011 and a whole package of austerity measures have been put in place by the government. This includes wage reduction for public servants, a huge tax raise, an increase in utilities and transport prices as well as in health and education costs, along with cuts in social benefits (including unemployment and health benefits).

Unemployment and the deterioration in labour conditions are the consequences of the entire restrictive policy that has been implemented and that led to a significant income reduction, especially for the middle class. The drop in investment (both public and private) and the decrease in consumption do not stimulate job creation and risk taking.

The economy is in deep recession, which will aggravate the financial stability of more and more households. The persistence of the economic downturn increases the risk of over-indebtedness for the years to come. This can be accelerated if the interest rates in the Eurozone start to rise. The low levels of interest rates have been attenuating the financial hardship for many families. It is worth highlighting that more than 90% of mortgages are contracted at variable interest rates.

IX. Micro-economic risk factors for over-indebtedness

1. What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)

In 2012, revolving credit products, which includes not only credit cards but also overdraft facilities and other lending facilities, was the credit sector that had a less pronounced reduction (6.9% les contracts when compared to 2011). In the first quarter of 2013, it even registered an increase in numbers. When compared to 2011, personal loans decreased around 20% in 2012 and car loans diminished 30%. In 2012, revolving credit represented 68.1% of the total number of consumer credit contracts, but only 30.1% of the amount lent.[26]

Personal credit, despite the reduction in the number of contracts concluded and the amount provided in the last years, continued to be the segment with the greatest share of total credit provided. Car loans lost relative importance since 2010. For revolving credit, where credit cards prevail, the reduction in

26 BdP, 2013c, Retail Banking Markets Monitoring Report, available at http://clientebancario.bportugal.pt/pt-PT/Publicacoes/RAM/Biblioteca%20de%20Tumbnails/Retail%20Banking%20Markets%20Monitoring%20Report%20(2012)%20-%20Introductory%20Note.pdf.

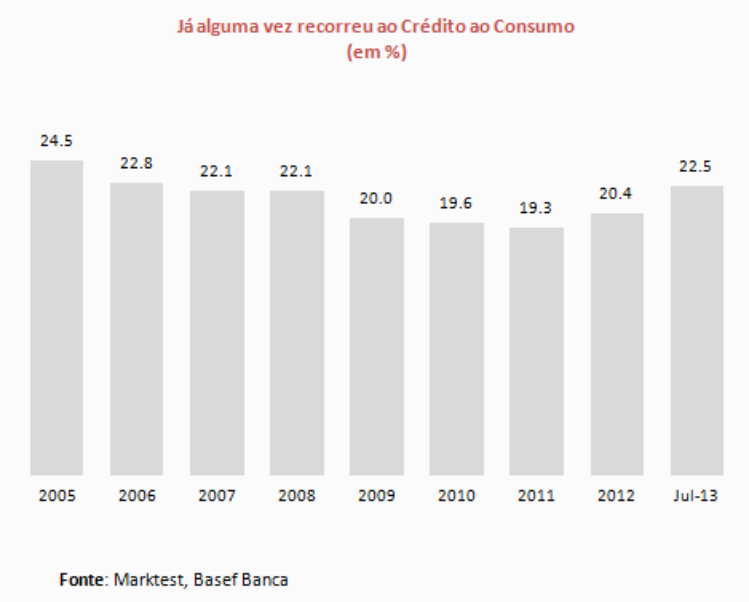
the number of contracts concluded and the credit provided was not so important. In 2012, the amount for revolving credit exceeded that for car loans.[27] When we look at over-indebted households, personal loans and credit card loans also surpass car loans. With the crisis, car loans fell sharply while personal loans and credit cards rose.

According to the OEC/DECO survey, until 2007/2008 the access to basic assets was the main cause for applying to consumer credit (including mortgage). Since then, there was a shift in the motivations: the top two became to *deal with current financial difficulties* and *to repay other loans*. This shift is in line with the increasing importance of personal loans and credit cards.

2. How many credit agreements do consumers conclude on average?

The information available does not allow us to estimate the required information. However, we have the data from the surveys' company Marktest showing how many Portuguese individuals have already had at least one consumer loan. The sample is formed by individuals over fifteen years old who possess a bank account and live on the mainland (Chart 4).

Chart 4 – Number of individuals that have had resorted to consumer credit (%)



Source: BASEF

The number of Portuguese individuals using consumer credit decreased between 2005 and 2011, although this seems to have been reversed in 2012 when 20.4% of individuals said they had resorted to this financial product.

The available data does not allow us to make assumptions about the reasons behind the shift observed since last year. However, we suspect that, with the current economic situation and rise of unemployment, combined with salary and social benefits cuts and with tax increase since 2011, many households are applying for new credit in order to repay other debts, including daily expenses and mortgages. If this is the case, and the steady increase in the number of bankruptcy files seems to confirm this suspicion, the default rate and the number of over-indebted households will continue to grow in the years to come.

The Bank of Portugal, in its Financial Stability Report of May 2013 stated that

27 Bank of Portugal (2013c).

> "in the first quarter of 2013 there were signs of a less noticeable contraction in the demand, especially in the case of consumer credit and other lending. The decline in consumer confidence and the negative prospects for the housing market continued to fuel the reduction in households' demand for loans (BdP, 2013a)."[28]

According to DECO's statistics, among over-indebted people the average number of credit contracts per over-indebtedness file was 4.6 contracts in 2012. This usually includes a mortgage credit, a car loan and several personal loans and credit cards.

3. Was/is the housing market in the country based on rent or ownership?

The Portuguese housing market is mostly based on ownership. The 2010-2011 Household Budget Survey reported 74.9% owned dwellings, 19.1% rented dwellings and 5.9% free lodging (INE, 2012).

4. How many mortgage agreements were concluded per year since 2007?

Between 1 October 2011 and 30 September 2012, 24,851 mortgage agreements were concluded, a 59.3% decrease when compared to the previous period of the same length, with an average amount of €83,891 (a 16.1% decrease when compared to the previous period of the same length) (BdP, 2013a). By the end of September 2011, there were 1,687,572 housing loans, while in the end of September 2012 there were only 1,617,735 active housing loans.

According to the European Credit Research Institute (ECRI, 2012), housing loans in Portugal reached €4,976 per capita in 2000, a value that had doubled by 2008 (€9,838 per capita).[29] In 2011, the amount was €10,606 euros per capita.

5. How many indebted and over-indebted consumers have credit card debt?

The data on credit cards is scarce and out-of-date. The data was published in 2012 and refer to 2011. They were produced by Marktest, a private market survey company. The subject group of the survey are consumers fifteen years of age or older, with a bank account, living on the mainland.

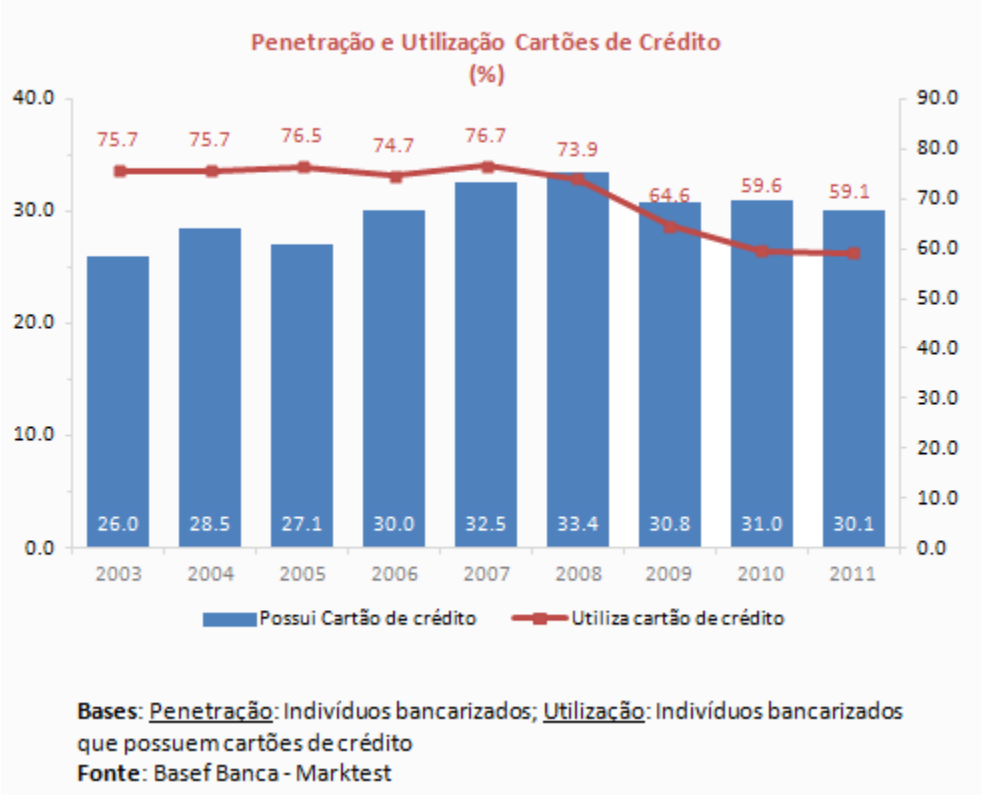
The Marktest survey accounts for 2,176 million credit card holders (with at least one credit card) in 2011, a number corresponding to 30.1% of that group. Only 59.1% of card holders actually use it. There seems to be a tendency for a decrease in credit card possession and use since the beginning of the financial crisis (Chart 5).

Recently, the ECB stated in its report that, on average, each Portuguese individual has 1.9 credit cards.

28 See Bank of Portugal (2013a), Financial Stability Report of May 2013, available at https://www.bportugal.pt/en-US/EstudosEconomicos/Publicacoes/RelatorioEstabilidadeFinanceira/Publications/REF_Nov_e.pdf.

29 ECRI (2012), Statistical Package on Lending to Households.

Chart 5 – Possession and use of credit cards (%)



Source: Marktest (http://www.marktest.com/wap/a/n/id~1976.aspx)

Legend: blue columns – credit card possession; red line – credit card use by the possessors

The limited possession of credit cards by Portuguese households seems to significantly contrast with the relationship between over-indebted consumers and credit card relationship. When considering the average number of credits by type of credit of over-indebted individuals supported by the consumer association DECO, we observe an average of 1.5 credit cards per individual/household for the first semester of 2013 (Table 7). Additionally, the data shows that 51.2% of over-indebted individuals requested assistance due to debts related to credit cards.

Table 7 – Average credit by type and credits restructured by DECO in 2013

Type of credit	Average credit by type of credit among over-indebted	Credit whose intervention of DECO was required (%)
Mortgage credit	0.8	27.5
Car loan	0.3	19.6
Personal loan	1.8	57.6
Credit card	1.5	51.2
Other credits	0.2	9.5

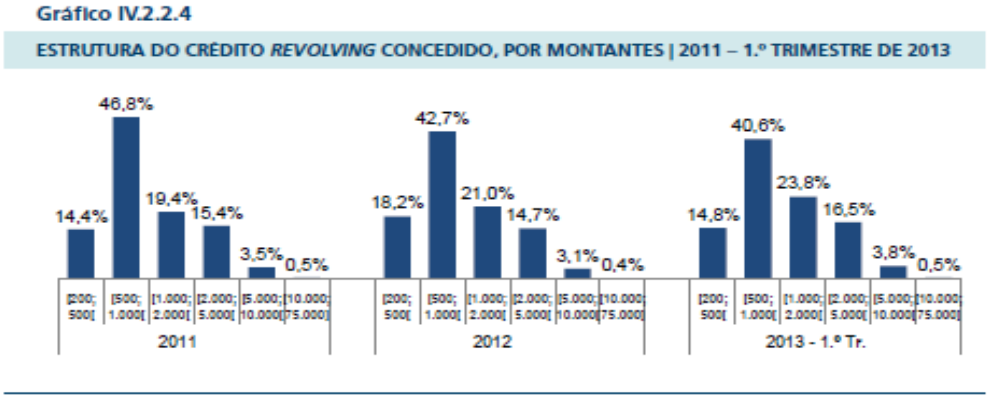
Source: DECO

a. *How high is this debt?*

In 2011, the average monthly amount for revolving credit contracts celebrated each month was €88,754 per contract, while, in 2012, that amount was only €80,804 and in the first quarter of 2013 it rose to an average of €88.106.

Within revolving credit, in 2011, about 80% of new contracts had ceilings up to €2,000 with the largest concentration occurring between €500 and €1,000. About 18% of the new revolving credit agreements presented had credit ceilings below €500. Values higher than €5,000 represented less than 5% of the total. Between 2011 and 2012, there was a reduction in the importance of contracts with ceilings higher than €2,000 (BdP, 2013c). See chart below (Chart 6).

Chart 6 – Amount of revolving credit, by year (%)



Source: BdP, 2013c.

b. How long does it take consumers on average to repay credit card obligations?

Although there is no statistical information available on the subject, the interviews allowed us to make two relevant observations. According to the respondent from the only banking institution that accepted to answer some of the questions, the majority of the bank customers (at least in the institution that is the major Portuguese bank) pay 100% of the credit card every month. This means that the card is used as a means of payment and not as a credit instrument.

On the other hand, 20 of the 27 over-indebted respondents who had credit card debts in arrears, have stated that it would take between five and eight years to settle the debts, according to the agreement that they had been able to negotiate with the creditor, with DECO's assistance. [30]

6. What percentage of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?

The only information available on overdraft facility comes from the 2010 Financial Literacy Survey conducted by the Bank of Portugal. According to the survey, only 25% of the individuals with at least one bank account said they have this type of credit. 56% did not have that facility and 19% did not

30 We conducted 29 semi-structured interviews in some of the offices of the consumer association DECO. We chose the individuals that accepted to be interviewed and that were there for any purpose related to consumer support. That made our sample distorted because the more frequent clients were over-indebted individuals (27 of 29 interviewees), and because these were more talkative. In past fieldwork with over-indebted consumers, we felt that in many cases they sought someone with whom they could share their stories without being judged. See Frade, Catarina et al. (2006), Desemprego e sobreendividamento: contornos de uma ligação perigosa, Coimbra: CES.

know if their bank account allowed overdraft facility. From those having overdraft facility, 38% said that never use it, 37% said that rarely use it and only 25% said that used it in a regular basis.

When asked about this type of credit, all 29 consumers showed themselves unable to recognise this financial product. Only when it was referred as "wage account"(conta-ordenado) did the respondents showed to know what it was. In their case, they did not use it or the bank had already removed this credit facility from them. According to the financial institution interviewed, the average interest rate practiced at that time by the institution for the overdraft facility was 11.45%. The institution only allows an overdraft equivalent to 80% of the value of the customer's monthly salary, although some banks reach 100% of this value. The interest payment has a deductible: exemption from the payment of interests during the first week, and up to a value of €250.

Since this type of credit is given mainly in the form of an advance in wages, most customers pay it as soon as they receive their salary. The bank is limited to automatically deducting the advanced amount and the corresponding interest. In some cases, however, it could mean a drastic reduction in income for the rest of the month, especially when the ceiling used is very close to the value of the monthly salary.

Since the start of the crisis, the financial institution has observed a new, sometimes contradictory dynamic in the use of credit cards and overdraft facilities. On the one hand, many clients have cancelled these financial products and on the other hand there has been an increased use by those who keep them. Financial institutions have also become more forward-looking, by either reducing the ceilings of the credit cards and overdrafts, or replacing the more selective cards by the more common ones (instead of golden credit cards, classic credit cards etc).

7. Is there a relation between the length of the credit obligation and over-indebtedness?

a. Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?

Data on the relationship between contract term and over-indebtedness is almost non-existent. The only available reference comes from Farinha and Lacerda, 2010.[31] These authors refer to the likelihood of entering into default increases as time passes, at least regarding loans contracted in recent years. However, this effect tends to disappear as the end of the contract approaches.

b. How long are the time periods for which consumers took on credit and mortgage obligations?

The initial term average for contracts of mortgage loans on 30 September 2012 was 30.9 years, of which 13.3% had a maturity not exceeding 20 years, 48% had terms above 20 years but a maturity equal or inferior to 30 years, and 38.7% were contracts with maturities of 30 years.

Credit agreements concluded between 1 October 2011 and 30 September 2012 have an average initial term of 31.6 years. Comparing the dispersion in contract terms within this period against the corresponding period of the previous year there is an increase from 33.9% to 43.5% in the number of contracts concluded with terms equal or less than 30 years (BdP, 2013a).

c. What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?

The Bank of Portugal has released some data on this subject in its interim overview of the Behavioural Supervision Activities (BdP, 2013d).[32] The data refers only to the enforcement of the new legal

31 Farinha, Luísa & Lacerda, Ana (2010) "Incumprimento no crédito aos particulares: qual é o papel do perfil de crédito dos devedores?" in Bank of Portugal, Relatório de Estabilidade Financeira Novembro 2010.

32 Bank of Portugal (2013d), Síntese Intercalar de Atividades de Supervisão Comportamental 2013, available at

regimes created in late 2012 like the PERSI regime. Most credit agreements incorporated into PERSI were concluded in the years between 2005 and 2010 (58.4%), involving a total amount of €4.5 billion of debt. In relation to mortgages, 59.5% of contracts subject to PERSI were concluded between 2000 and 2007. With regard to consumer credit, 64% of contracts within the PERSI were concluded over the last five years.

X. Relation between income and (over-)indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

According to the final results of the 2010/2011 Household Budget Survey (INE, 2012):

"the household annual mean consumption expenditure was 20,391 euros in 2010/2011. Housing, transport and food products accounted for 57% of the household annual mean consumption expenditure. The concentration in these classes of expenditure kept the pattern already observed in the previous decade, despite the increase of the weight of housing expenditures (19.8% in 2000 and 29.2% in 2010/2011) and the reduction of expenditures with food products (18.7% in 2000 and 13.3% in 2010/2011). The average net total annual income by household was 23,811 euros in 2009, corresponding to a monetary income of 19,811 euros (80.6%) and a non-monetary income of 4,910 euros (19.4%)."

A percentage of 57.0% breaks down to expenditures on housing (29.2%), transport (14.5%) and food and non-alcoholic beverages (13.3%). In 2010/2011, the average total annual expenditure of households with dependent children stood at €26,775, i.e. 31% above the global average (€20,391) and 60% above the average for households without dependent children (€ 16,705) (INE, 2012).

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

    a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate this risk through higher interest rates?*

According to the one financial institution interview we could conduct, banks usually consider low-income consumers riskier. In most cases, this means that they are not considered eligible for credit.

    b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

In the few cases where they are granted the loan, the spread is much higher than for other customer segments and more collateral (like guarantors) is required.

    c. *Are there other key terms which change according to the income of the borrower?*

Low-income consumers usually have access to lower amounts of credit. While a high-income consumer may obtain 100% of the house price from the bank, a low-income is unlikely to obtain a loan of 75% .

(Contd.)

http://clientebancario.bportugal.pt/pt-PT/Publicacoes/RSC/Biblioteca%20de%20Tumbnails/S%C3%ADntese%20Intercalar%20de%20Atividades%20de%20Supervis%C3%A3o%20Comportamental%20(2013).pdf.

Behaviour of actors in relevant cases

XI. Irresponsible lending practices

1. Who was the initiator of the relationship between creditor and borrower?

Regarding mortgage credit, the initiative belongs mostly to the debtor, but many real estate agencies act as intermediaries in several contracts for their clients. Until September 2002, the government promoted housing purchase through the subsidized credit regime. As for consumer credit, lenders usually take a more proactive role: they offer credit cards and personal loans by phone or in malls and supermarkets.

Advertising is still very intense in both types of credits, even today.

2. Was a creditworthiness assessment undertaken before granting the credit?

a. In how many cases were creditworthiness assessments undertaken?

There is no available data on this issue. However with Decree-Law 139/2009, consumer creditworthiness assessments became mandatory for consumer credit loans. According to the bank employee interviewed, the respective financial institution's policy regarding household credit demand (both mortgage and consumer) is to always make a creditworthiness assessment. Creditworthiness assessments are more restricted within mortgage credit. For this assessment not only is the information provided by the debtor relevant but so too is their historical path with the institution and their register in central bank database (credit bureau).

b. Who was the initiator of the creditworthiness assessment?

The initiator is always the financial institution.

c. Who undertook the creditworthiness assessment?

The financial institution.

d. What were the criteria of the creditworthiness assessment?

Financial institutions do not reveal their criteria but it is known that the debtor's monthly income, current loans, the debtor's and debtor's partner's professional situation (including the stability of the employment relationship) and the past relationship between the debtor and the financial institution are some of the key elements taken into account while examining a debtor's risk profile.

e. Was a credit bureau involved?

As stated before, with Article 10 of the Decree-Law 139/2009, consumer creditworthiness assessments became mandatory. However, this does not mean that creditors are compelled to consult a credit bureau. They can simply rely on the information provided by the debtor.

However, if the client is a usual client, the creditor has immediate access to their credit records because the database of the Bank of Portugal provides regular information to credit institutions on their clients. If it is a new client, the creditor needs the permission of the client to access the Bank of Portugal's database.

3. Is there a legal obligation for a mandatory creditworthiness assessment? Is this obligation observed in practice?

According to the Decree-Law 133/2009, of 2 June 2009 banks are obligated to assess the creditworthiness of consumers before granting credit. In addition, Notice 17/2012 of the Bank of Portugal establishes that, when a situation is related to the prevention of non-compliance of credit agreements and it is necessary to assess the financial capacity of the consumer, credit institutions should collect the data specified in that notice in order to assess the creditworthiness and financial

capacity of borrowers. There is no available data about compliance with this obligation in practice but indirect evidence suggests that, at least in mortgage credit, this is a regular practice.

4. *Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?*

According to Costa and Farinha (2012), based on the 2010 Household Financial Situation Survey:

"among the families who requested credit, about 20 per cent saw their applications refused or only partially satisfied. The higher incidence of these situations have occurred in families with lower income, lower wealth or where the reference person is unemployed, has a contract term employment or age classes are younger or older."[33]

5. *Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?*

There is a legal obligation upon creditors to disclose information regarding the consequences of failure, which was reinforced by Decree-Law 227/2012. According to our consumer interviewees (27 over-indebted and two indebted consumers), 21 claimed that the financial institution did not alert them to the consequences of failure to meet repayments. Five consumers revealed that these clarifications were granted only after the default occurred and only three of them said they had been informed before the conclusion of the contract. In most cases the information relies on the documents signed by the consumer, but either they did not read it or fully understand it. In addition we must be aware that our sample is mostly based on over-indebted individuals. As we have realised in previous fieldwork, consumers in financial stress tend to blame someone else for their situation (specially the banks).[34]

6. *Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?*

Our consumer interviewees expressed very different perceptions about financial institutions behaviour. Some of them felt some pressure to sign the contract, while others said that they had not felt any special pressure. There seems to be a connection between these perceptions and the fact that the financial institution was or was not the regular bank of the consumer. People seem to feel less pressured when they are dealing with their bank and above all, with an employee with whom they are familiar. Some empirical findings on a current research project show that consumers tend to very much trust the bank employee in charge of their account. [35]

XII. Irresponsible borrowing practices

1. Did the consumer read the agreement before signing?

According to the 2010 Financial Literacy Survey, conducted by the Bank of Portugal (BdP, 2010), 74% of the respondents said that they read in great or some detail the information provided by the financial institution when they are about to contract a loan or make an investment decision, while 15% declared not to have read the information.

33 Costa, Sónia & Farinha, Luísa (2012), O endividamento das famílias: uma análise microeconómica com base nos resultados do Inquérito à Situação Financeira das Famílias, in Bank of Portugal, Financial Stability Report, May 2012.

34 See Frade, Catarina et al. (2006), Desemprego e sobreendividamento: contornos de uma ligação perigosa, Coimbra: CES; Frade, Catarina et al. (2008), Um perfil dos sobreendividados em Portugal, Coimbra: CES.

35 See the research project BEHAVE – a Behavioral Approach to Consumer Credit Decision-Making (http://www.ces.uc.pt/projectos/behave/pages/pt/projeto/destaque.php).

This data must be interpreted with caution because the question refers to all information (including brochures and booklets) and not only to the contract. Moreover, the effect of "politically correct answer" may have distorted the results.

Additionally, even if the results reflect reality, this does not necessarily mean an understanding of the information provided, as other indicators on the survey confirm.

2. *Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?*

The 2010 Financial Literacy Survey shows that, with regards to the investment of savings, 56% of the respondents declared not to make comparisons, while with regards to loans the percentage decreases to 40%.

3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*

Of our 29 interviewees, eight stated that the bank had provided the opportunity for consumers to read the contract and to ask questions before signing the agreement. Ten revealed that the bank had not given them such opportunity, although they had asked for it, while five reported that the bank only allowed for reflection time and clarifications in mortgage loan contracts. Finally, five interviewees said they did not ask for any clarifications and one consumer did not recall the situation.

4. *How much time did the consumer take before signing the agreement?*

According to the interviewees, eight consumers revealed that they had taken two or three days before signing the contract. The other 21 consumers said that they had signed the contact immediately.

5. *Do consumers make use of the right to withdraw?*

The withdrawal period is fourteen days. No statistics are available but according to the bank employee interviewed this right is rarely used.

Litigation

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*

Commentary regarding the litigation in Portugal on consumer and housing credit results from interviews with four judges - two from first instance courts and two from the Courts of Appeal of Lisbon and Porto - as well as two lawyers, one of whom is also a member of a consumer defence association. With these interviews we tried to overcome the shortcomings of the official statistics on justice and also form an idea of the key trends and dynamics of litigation involving consumer and housing credit.

Semi-structured interviews were conducted, based on the script of the project. In three cases, the responses were obtained in person, while the remaining responses were given in writing. A number respondents were asked further clarification. The content analysis of the responses shows common perceptions between all respondents in various aspects but also shows some differences. These differences are visible between the first instance and appeal court judges and also between judges and lawyers.

   a. *What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?*

Research based on the Ministry of Justice database shows only a few cases based in consumer credit law (Decree-Law 133/2009) decided by the courts of appeal. However, we are unable to draw a precise picture of the litigation because the decisions of the first instance courts are not available in the database.

The interviewed judges point out as a fundamental reason the unpreparedness and lack of knowledge of lawyers about consumer law. The lawyers who were interviewed, while recognising that consumer law is still little known and used and that many lawyers continue to use the general rules of civil law that are less protective of consumers, claim that there have been improvements in the dissemination and application of consumer law.

Thus, the proceedings where the debtor seeks the annulment of the consumer credit contract based on purely formal issues, such as failure to deliver a copy of the contract, breach of the disclosure duty on the general contractual clauses by the lender, the excess of the indemnity clauses, or the right to automatic termination of the contract based on a single default with immediate payment of subsequent instalments, persist. In these cases, the lawyers invoke the abuse of rights to try to challenge credit contracts and to justify the default. While the first instance judges consider that the majority of proceedings are decided in favour of the lender (since this is an enforcement order), the court of appeal judges said that the favourable decisions for consumers have increased. In 44 cases decided by the courts of appeal we reviewed, only fourteen were decided in favour of the financial institutions. These two perceptions are, however, compatible, since the cases in which there is appeal are a minority compared to the amount of cases decided by the first instance courts.

Besides these perceptions we may outline further scattered information to complete the picture further. Although consumer law has existed for a long time (since 1996), courts are very conservative when it comes to consumer conflicts. Surprisingly, the same happens in consumer arbitration centres according to an unpublished report of the General-Directorate for Consumer Affairs. In both cases, judges tend to apply general contract and tort law – including the regulation of abusive clauses prescribed under Decree-Law 446/85, 25 October 1985 - more often than consumer law.

Thus, besides the use of the general scheme of standard contractual terms (Decree-Law 446/85 of 25 October 1985) it is also common to refer to the general civil law institutes, namely, regarding the abuse of law (Article 334 of the Civil Code) and the expiration of benefits due to default (Article 781 of the Civil Code). Court decisions are also very variable regarding the assessment of these institutes. For example, the Court of Appeal of Lisbon (judgment of 22 October 2009) considered consumer behaviour as an abuse of law (*venire contra factum proprium*), by invoking the nullity of the contract, due to the lack of delivery of a copy of the contract when there are already several settled instalments. On the other hand, the Court of Appeal of Coimbra (judgment of 4 May 2010) considered that the borrower's act when invoking nullity for lack of delivery of the contract's copy is not an abuse of right, even if the borrower has already partially complied with the contract (the jurisprudence of the Supreme Court has followed this direction, in judgments of the 30 October 2007, 28 April 2009, 2 June 2009 and 1 January 2010).

b. What were the issues in question? (i.e.: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?

According to 44 Appeal Courts decisions analysed the main issues in question were:

- Pre-contractual and contractual information duties
- Delivery of a written copy of the contract to the consumer
- Abusive clauses
- Tied contracts (credit contract associated to a selling contract)
- Aggressive selling

According to data from the Ministry of Justice, between 1995 and 2012, there were 230 judgments of invalidity of abusive contract terms across the three courts levels (first and second instance courts and Supreme Court), involving banking and insurance, where standard contracts are common. 2007 was the year that registered the highest number of cases (44). This unusually high number is associated with the publication of Decree-Law no. 240/2006 of 22 December 2006, which established the rules for rounding the interest rate of the mortgage contracts. According to this law, it became mandatory to round the interest rate to the nearest thousandth in the mortgage contracts. Many credit institutions had not changed their standard terms accordingly in a timely manner (maintaining the rounding to the quarter or more).

2. *Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?*

Individual plaintiffs are dominant. However, organisations like consumer associations have the right to initiate judicial procedures (Article 60 of the Portuguese Constitution).

3. *What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?*

Regarding the 44 cases of the Courts of Appeal analysed, in only fourteen cases were the decisions favourable to the financial institutions.

4. *Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?*

If yes:

   a. *How are those interests defined?*

Article 52 of the Portuguese Constitution enshrines the right of all citizens to submit, individually or collectively, to the organs of sovereignty (including the courts) or any authority petitions, representations or complaints to protect their rights, the Constitution, the law or the public interest. There is a difference between diffuse interest and collective interest:

- *Diffuse interest* is the reflection at each individual unit; interest is here considered in a community and a global perspective.
- *Collective interest* is a particular interest common to certain groups and categories.

   b. *What are the requirements for such representation?*

The organisations or consumer associations must fulfil the following requirements, they must:

- Have legal personality
- Must include expressly in its duties the protection of interests concerning popular action
- Cannot exercise of any professional activity competing with companies or professionals

5. *In practice, is litigation in "public / diffuse interest" more common than individual litigation?*

No. Individual litigation is by far the most common.

6. *Does the national legal framework allow for out-of-court settlement procedures?*

Yes. The national legal framework allows out-of-court settlement procedures and there is currently a large effort to implement even more alternatives to the already existing ADR procedures. The consumer law (Law 24/96, 30 July, 1996), under the Article 14 prescribes the duty of the Government to promote and support ADR procedures related to consumer issues.

Additionally, some arbitration centres for consumer issues were created in the 1990s. In 2000, the main consumer association, DECO, created its Over-indebted Supporting Offices (GAS), which have had an important role in out-of-court settlements procedures related to consumer and mortgage credit issues.

In 2010, the Government created the Credit Mediator, an office installed at the facilities of the Bank of Portugal. Its initial aim was to settle the conflicts of consumers who saw their credit request denied by the bank. Very quickly, this purpose was put aside since the office started to receive requests for support from consumers in financial difficulties. Although the number of files dealt with is very low compared to DECO's (around 200 files per year) this is another option available to consumers. This office is also involved in the new regime of PERSI.

Corporations and other smaller consumers associations or civil society organizations have been involved in the issue of extrajudicial support to households in financial distress.[36]

7. Do consumers make use of out-of-court settlement procedures?

If yes:

a. Which ones?

Usually, consumers use the existing normal ADR procedures, including the over-indebted supporting offices (GAS) created by the Consumer Portuguese Association (DECO). However, as already noted, there are now new alternative means of resolving disputes that enable regularisation of credit defaults (PERSI).

b. What is their success rate?

According to DECO, this Portuguese Consumer Association has a 70% success rate.

Very recently, the Bank of Portugal published the first results of the new legal regimes established by the end of 2012: PERSI regime and the regime for households in a harsh economic situation (BdP, 2013d).

Concerning *PERSI*, the data shows that 573,732 files were received by financial institutions between January and June 2013 – 446,471 related to consumer credit and 127,261 to mortgage credit. Only 32.3% of the total files resulted in the repayment of the amount in arrears or in a new agreement between creditor and debtor. The success rate was higher in mortgage credit (41% of the 127,261 files received by all the financial institutions) than in consumer credit (29.9% of the 446,471 files received). In the first half of 2013, two reasons for the extinction PERSI procedure stood out: the lack of agreement between the parties (60.5%) and the payment of the amount in arrears (25.7%).

The *regime for households in a harsh economic situation* is far from being so noticeable. Between November 2012 and June 2013, the entire financial market (20 institutions) received 1318 cases in total. Out of these, 944 (79.3%) were rejected because the debtors did not fulfil the legal requirements (Law 58/2012). Of the files approved (247), only 108 were finished and 84 were successfully concluded either by the payment of the amount in arrears or by a new agreement between creditor and debtor.

8. Are there special bankruptcy courts? What is their role?

No. In some cities, however, there are commercial courts competent to deal with corporate bankruptcies (but not private individual cases).

36 More details are available in Eurofound's 2012 report on debt advisory services (available at http://www.eurofound.europa.eu/pubdocs/2011/89/en/1/EF1189EN.pdf).

XIV. Impact of the crisis on litigation

1. Has there been an increase in litigation since the financial crisis?

The general perception of the judges interviewed is that litigation relating to *mortgage loans* has not increased and remained scarce, as it was in the past (more details below)..

In *consumer credit*, judges have felt some increase in litigation since the crisis outbreak.

a. How many mortgage agreements where challenged in out-of-court or judicial proceedings before and after the crisis?

The out-of-court proceeding where we can see mortgage loans being dealt with is the aforementioned regime established in 2012 for consumers in *harsh economic situation* owing a mortgage. We already stated that this regime has been scarcely relevant in current economic situation of households. In April 2014 the government announced its intention to revise this law and relax the conditions of access to the scheme. So far we do not know what changes there will be.

According to the judges interviewed, there was no increase in litigation regarding mortgage agreements. The number of files is scarce even after the outbreak of the crisis (2008/2009) in relation to the declaratory component. However, judicial collection proceedings and insolvency files associated with housing and consumer credit saw a large increase. This divergence stems from the difference in position and power of the parties. The lender, typically a credit institution, resorts more easily to court than the borrower. The lender usually not only possesses a legal office specializing in collections, but is usually also provided with a personal or real guarantee (e.g. the mortgage) or an enforcement order (e.g. a promissory note) that does not require prior initiation of a declaratory proceeding with the risk of discussing the validity of any contract term. On the other hand, borrowers, typically a consumer or a family, do not have the same legal resources at their disposal and lack the financial means to fund the litigation against the lender. More often than not, the borrower or debtor is not even aware of the potential unfairness of some contractual terms (nor do they fully understand the contents of the contract). Thus, the increase in judicial collection and insolvency proceedings did not bring an increase or deepening of the discussion on the substance of credit contracts, neither in policy nor in jurisprudence.

b. What are the issues challenged? In which legal field?

The regime established in 2012 for consumers in a "harsh economic situation" owing a mortgage, as out-of-court proceeding, deals only with the measures capable of rectifying the arrears. No substantial issues are discussed in it.

With regards to judicial proceedings, there is a lack of case law concerning mortgages. However, two judgments deserve attention. In January 2012 a trainee judge caused a series of legal and political comments and newspapers articles due to his decision to deny a bank the claim for the remaining debt not covered by the amount obtained through the sale of a house and transferred in lieu of payment. In the case, the debtor had delivered the house to the bank, which soon after advocated its judicial sale. The bank was the buyer of the house for an amount lower than the value of repossession fixed by the bank when the transfer in lieu of payment occurred. The judge denied the collection of the difference of the value to the bank claiming that this collection represented an abuse of right and an illicit enrichment of the creditor. The bank appealed this ruling, but the Court of Appeal of Évora (Tribunal da Relação de Évora) denied the appeal on the grounds that it had been brought out of time. This decision was influenced by the decisions of Spanish Court of Navarra in 2010, which was highly discussed in Portugal (even though these decisions had been overruled in the Courts of Appeal). This decision of Portalegre Court occurred in a very specific context that can hardly be repeated: in a inventory process following a divorce. The inventory process used to allow (not anymore) meeting substantive issues, as it happened in this case.

In a similar case before the Court of Appeal of Lisbon, in a decision of October 2012, the judge disagreed with the decision of Portalegre, saying that there was no abuse of right from the bank by claiming the remaining amount and refusing the perspective adopted by the Court of Portalegre, as well as the Spanish Courts of Navarra (2010) and Barcelona (2012).

It is surprising that, given the current economic crisis in the country and the importance of mortgage loans, litigation about mortgage lending remains scarce, especially with regard to the discussion of contractual conditions and their equity.

2. Did the Aziz ruling have an impact on national legislation / legal framework?

a. Are there cases before national courts dealing with issues that also arose in the Aziz case?

All the judges interviewed recognised the little or no influence that the *AZIZ* process and also the sentences of the Spanish courts have had in the decisions of the Portuguese courts. Two reasons were pointed out.

First, housing credit is only discussed in the context of judicial collection or insolvency procedures, and not declaratory procedures and as such there is no place for any in-depth analysis that can jeopardise the validity or reasonableness of the terms of the contract. The bank merely resorts to the judicial collection or insolvency, so there will not be a discussion as to the value of the property or the possibility of transfer in lieu of payment.

Second, due to the economic crisis in Portugal, there is an almost total absence of housing credit being granted. In fact, there are not many people interested in judicial collection sales, even though the houses are advertised for sale at an attractive price. This enables the mortgage creditor to claim property auctioning for a low amount. Since there is no proposal from a third party to cover the value offered by the bank, the property is awarded to the bank for a lot less than the actual value. As a result, the borrower loses the house and still owes the bank a substantial part of the debt.

According to some of the judges and one of the lawyers interviewed both jurisprudence and doctrine consider that it is very difficult to avoid this issue because of the rules that the Civil Code provides for on fulfilling obligations: a) the fulfilment of the obligation account for all the debtor's assets (Article 601 CC); b) when the property is sold and part of the debt remains, the creditor can pledge other assets of the debtor.

This position of judges is rather conservative. The Supreme Court in its judgment of 10 October 2013 held that

> "the resolution or contract modification for changed circumstances depends on the fulfilment of the following requirements: (i) there is a material change, ie abnormal circumstances in which the parties have established a hiring decision and (ii) a requirement to fulfil the obligation to the injured party seriously affects the principles of contractual good faith and are not covered by business risk."

This approach of the courts is in line with the stance of the doctrine that has difficulty recognising a more active role of clauses that may modify the terms of the contracts, as the change of circumstances, the unforeseeability or the force majeure. According to Monteiro and Gomes (2006), "the problem of establishing the legal relevance of supervening alteration in circumstances is an old preoccupation in Portuguese Law" (see above at V.5).

b. What was / is considered an unfair contract term in the national court rulings before and after Aziz?

Since Aziz case had no impact at national level, the concept of unfair contract term remained unchanged. Regarding the type of clauses that have been declared unfair, some of them are related to the exclusion of the right to claim or action and the allocation of costs and charges for the collection of the monthly instalments (e.g. case 813/09.8YXLSB, 2nd Civil Court of Lisbon), to amend the rules of

risk or burden of proof as to the unlawful use of credit card (e.g. process 2900/12.6TJLSB, 4th Civil Court of Lisbon), the insertion of clauses "after the signing of contractors" (e.g., process 40336/12.6YIPRT and 1166/10.7TJLSB, 4th Civil Court of Lisbon), the loss of period benefit (e.g., process 8186/11.2TBOER, 3rd Civil Court of Oeiras) and the rounding (up) of the interest rate on housing credit (e.g., process 516/10.0YXLSB, 4th Civil Court of Lisbon).

One of the judges interviewed said that it was common that, after a contractual clause has been repeatedly declared unfair, many financial institutions altered or eliminated it, creating, in its place, a new clause through which they intended to obtain a similar result or compensation for losing the previous clause. Thus, they tried to avoid the illegality purpose, while obtaining a similar effect. This makes, in the expression of other respondents, the standard contracts such as credit ones contracts increasingly "armoured contracts" which greatly hinders the ability of the debtor to challenge them in court.

c. *Did Aziz have any other impact on national legislation / legal framework (i.e. in the field of procedural law)? What are those impacts?*

There was no impact.

3. *Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework?*

No.

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

Yes. As already noted, in 2012, the regulatory authority approved several bills aiming at the protection of households in financial constraints. The main focus lies on mortgage credit default but the limited criteria to access the regime precludes the efficiency of the initiatives.

Another important initiative is the 2011-2015 *National Plan for Financial Education* (PNFF)(http://www.todoscontam.pt/SiteCollectionDocuments/NationalPlanforFinancialEducation.pdf). This is the first integrated public initiative in the field of financial literacy and it is the result of a partnership between the Bank of Portugal (BdP), the Portuguese Securities Market Commission (CMVM) and the Insurance and Pension Funds Supervisory Authority (ISP). According to the report presenting the initiative,

> "The PNFF intends to contribute to increase the level of financial knowledge of the population and to promote the adoption of appropriate financial behaviours, through an integrated vision of financial education projects and through the combination of the efforts of the stakeholders, thus contributing to increase the wellbeing of the population and the stability of the financial system."

2. *Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?*

Consumer and mortgage law were changed in 2012. In 2011 the financial supervision of the Portuguese Central Bank was also reinforced. Bankruptcy law was modified in 2012 but only regarding companies.

3. *What are the changes in particular? Focus on consumer credit and mortgage law.*

Consumer law (Law 24/96, of 31 July 1996) was amended in 2013 by Law 10/2013, of 28 January 2013, in order to reinforce information duties of financial creditors.

Mortgage law was the subject that captured the attention of the regulator authority (it is worth bearing in mind that 80% of consumers' indebtedness is related to housing – see question II.4): the Decree-Law 227/2012 (concerning the PERSI) and Law 58/2012 (households with mortgage credit living in a harsh economic situation) were already mentioned.

Other bills deserve to be mentioned:

- - Law 57/2012, of 9 November 2012, allows consumers to mobilise education and retirement saving plans to repay mortgages without losing the tax benefits previously obtained through them and without suffering any penalty for early mobilisation.
- - Law 59/2012, of 9 November 2012, which amended Decree-Law 349/98, of 11 November 2012 (regulating housing credit), protects the debtor with a mortgage by forbidding the creditor to terminate the contract before three instalments are in arrears. Further, the creditor cannot increase the credit cost (including the spread) when the debtor rents their house because they become unemployed or have to move for professional reasons to another place or when they divorces or becomes a widower (and the person solely responsible for the mortgage) and the household effort rate is lower than 55% or, if there are children, 60%.
- - Law 60/2012, of 9 November 2012, which amended the Code of Civil Procedure by modifying the rules governing the order of the seizures and the determination of the base value for the sale of properties in the foreclosure process. The *sale value* must be at least 85% of the *base value* of the property to be sold.[37] The seizure of the house can only occur after the seizure of other assets.

Financial supervision was reinforced following the ECB rules. In January 2011, the Portuguese Central Bank (BdP) created the Banking Conduct Supervision Department (DSC), following the revised Legal Framework of Credit Institutions and Financial Companies, published in the Decree-Law No. 1/2008 of 3 January 2008. The regulating, monitoring and sanctioning tasks of BdP have been reinforced in order to ensure compliance with the principles of information transparency and accuracy, as well as with the law and regulations regarding retail financial markets and service provision.

4. *When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

The changes in consumer and mortgage law were due to the grave financial situation of households resulting from the crisis. Some of them were also forecast by the Memorandum of 2011 signed between Portuguese government and the troika (IMF, ECB and EC).

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, i.e. with regard to savings?)*

Yes. Some aspects worth highlighting:

- Concerning indebtedness, it should be pointed out that the credit market expanded relatively late in Portugal. It was not until the beginning of the 1990s that financial institutions discovered the

37 The base value is the highest of one of the following values: market value of the property or the taxable patrimonial value.

potential of the household sector. At that time, unemployment was at a very low level, salaries were raised, interest rates fell and commerce expanded as never before. At the same time, the demand for credit from companies was decreasing. This environment favoured the democratisation of credit to various socio-economic strata, especially for those with a high or medium to high income. Consumer indebtedness was also promoted by public policies, especially in terms of housing. The freezing of rents for decades led to the stagnation of the rental market and meant that buying a house was cheaper and fed the feeling of paying for something that was their property. The housing policy also helped this state of affairs, since government subsidised mortgages for low and medium income households, and offered fiscal advantages for those paying a mortgage. Municipalities were very fond of building investments because of the taxes and fees collected and the increased budget.

Until recently, consumer credit was mostly related to car loans. There was a renewal of the national fleet since the 1990s and the high cost of vehicles made credit the best solution for a household to acquire its first and second car. In the last two years personal loans became more common that car loans and this is a disturbing symptom of the current financial difficulties faced by many Portuguese families. Personal loans are often being used to repay other credits.

- Concerning over-indebtedness, the most worrying situation is related to the constant rise in unemployment, combined with the decrease in social benefits for unemployed and retired people. Portugal is a good example of what sociologists call a weak welfare State combined with a strong welfare society model. The welfare state was always less protective than that of northern Europe and its weakness was attenuated by informal networks of civil society based in kinship relations and relations of affection. Parents, other relatives and friends used to help households in financial hardship by providing them with assets (food, clothes, child care) and money. This solidarity effort helped many families in the past (as it still does today) to stay social and financially included. Many parents depended on their savings and on their retirement benefit to provide support to their children and grandchildren.

  Today, the issue is that, with the growing number of unemployed individuals, frequently belonging to the same family, and the cuts in retirement benefits, the welfare society is reaching or even surpassing its capacity to accommodate all the recent financial shocks. This means that the number of those defaulting and over-indebted individuals will continuously rise in the near future. And this is happening in a time where public expenditure is being significantly cut (e.g. public servants' salaries, and social benefits), and taxes being increased. This creates a social problem the proportion of which is being neglected.
- On savings, it is worth remembering that in the 1970s and 1980s, Portuguese households had savings rates higher than 20% of their disposable income, but this changed in the last two decades because of favourable economic conditions and the decrease of risk perception towards the future. In 2007, savings rate reached 8%, the lowest value in decades. Since then, there has been a slow increase in savings, showing a precautionary attitude of consumers. According to the National Statistics Office (INE, 2013), in December 2012, savings rate was 11.6%, in March 2013 it rose to 12.9%, and in June 2013, it reached 13.6% (household disposable income fell 0.2% in March 2013 and 0.3% in June 2013). In the last decades, some households invested in more risky financial products (like hedge funds) but the bulk of the families always preferred less risky solutions, like time deposits.
- The spending habits also changed, mostly within the middle class. Since the 1990s, the expenditure in food and beverages was decreasing, while transport, health and leisure spending increased. Nowadays, food expenses are rising because, with a lower income, people are focusing on essential expenditures. At the same time, the visits to restaurants fell sharply and people are cooking more often at home. There has been a decrease in fuel consumption (people travel less, especially for recreation purposes), leisure and culture, clothes and shoes.

- As for poverty, on 24 March 2014, the National Statistics Office (INE) published the provisional data from the survey of Income and Living Conditions (EU-SILC) conducted in 2013, relating to 2012. Below are the main results that show, in general, an increased risk of poverty in the country and the increase in social inequalities.

The risk of poverty (defined as a monthly income of less than €409) affected, in 2012, 18.7% of the Portuguese population (almost 2 million people), whereas in 2011 this value was 17.9%. This is the highest rate since 2005, when it reached 19%. Without social transfers from the State, that rate would rise in 2012 to 46.9% of the population resident in Portugal.

Teenagers under the age of 18 years old, couples with dependent children and unemployed individuals are the most vulnerable groups.

Thus, 24.4% of young people up to 18 years old are at risk of poverty (2.6 percentage points more than in 2011).

Families with dependent children registered an increase of 1.7 percentage points in its risk rate, to 22.2%. The rate reaches 40.4% among families with three or more children and 33.6% in the case of single-parent families. On the other hand, the risk of poverty among families without dependent children decreased from 15.2% to 15%, the same happening with households consisting of three or more adults without children, which have the lowest poverty rate, 12%.

Taking into account the labour situation, the risk is higher among unemployed people, with the rate rising 1.9 percentage points to 40.2% in comparison to 2011. And those who are employed also saw this risk increase in 2012 (0.6 points more, to 10.5%).

One in ten individuals was considered in severe material deprivation (10.9% of the population, when in 2011 this value was of 8.6%).

Considering only the income from employment, capital and private transfers, 46.9% of the population resident in Portugal would be at risk of poverty in 2012 (45.4% in 2011). This risk drops to 18.7% after social transfers.

While the richest 20% have six times more income than the poorest 20%, the richest 10% in Portugal have incomes almost eleven times greater than the poorest 10%. The INE concludes that in 2012 a strong inequality in the distribution of income was maintained, while the asymmetry in distribution between the population groups with greater and fewer resources "maintained the growth trend seen in recent years".

SPAIN

Pablo Gutiérrez de Cabiedes Hidalgo and Marta Cantero Gamito

Preliminary information

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial/consumer protection authority, etc.)?*

The terms "indebtedness" and "over-indebtedness" are not defined in the Spanish national legal framework (neither in the legislation, nor in the national case law).

"Indebtedness" is mentioned in the Spanish Bankruptcy Law (Law 22/2003, of 9 July) in Article 2 which requires the existence of an economic prerequisite for the debtor filing a bankruptcy procedure, stating in paragraph 3:

"If the application for a declaration of bankruptcy is filed by debtor, he must prove its indebtedness and insolvency, which may be actual or imminent".

This term is also used by the recent Law 1/2013 of May 14, on measures to reinforce the protection to mortgage debtors, debt restructuring and social rent. Its First Final Provision (Disposición final primera) exceptionally allows (in the two years following the approval of this Act) the possibility to request the payment of pension plans in case of foreclosure proceedings on the main dwelling (in order to prevent the auction). It also entitles the Government to extend the two-years period "taking into account the needs of disposable income given the situation of indebtedness arising from the circumstances of the economy" (emphasis added).

The term "over-indebtedness" has not been even mentioned until quite recently in the national legal framework; it has been specifically mentioned (but not precisely defined) in the Explanatory Memorandum of the recently approved Royal Decree-Law 27/2012 of 15 November on Urgent Measures to Reinforce the Protection of Mortgagors. This legal text merely explains the regulation and does not address the (complete) legal treatment of this problem, but only some of the most serious social effects of foreclosures.[1]

There is a lack of consensus on what over-indebtedness is. An exhaustive and systematic treatment of the issue can be found in a book on this matter that resulted from a study requested by the Spanish Consumer Protection Authority.[2] In that study, over-indebtedness is defined as

"a situation of financial hardship caused by excessive debt assumption in relation to income and current disposable assets. But that primary sense … must be qualified to be accurate and efficient, with a content … more determined: the difficulty of dealing with contracted debt; this is, to be in a situation

1 The Royal Decree-Law states: "Without prejudice to the need to address a more profound reform of the legal framework of treatment for individuals in situation *of over-indebtedness* and, in particular, to analyse improvements on the foreclosure proceedings, at this time it is required immediate government intervention to ease the most serious social circumstances that has been occurring"(emphasis added).

2 Gutiérrez de Cabiedes, P., El Sobreendeudamiento doméstico: prevención y solución. Crédito, crisis económica, familias y concurso, Thomson-Reuters-Aranzadi, Navarra, 2009, pp. 24-32 [HouseholdOverindebtedness: Prevention and Solution. Credit, Economic Crisis, Families and Insolvency].

of such a degree of acceptance of payment commitments that injures or threatens the ability of adequately and orderly pursing the obligations required of a person or entity".

The study also explains that over-indebtedness is different from insolvency. Over-indebtedness makes reference to a mere fact or financial situation (level of indebtedness being the ratio of debt relative to disposable income or assets), affecting the debtor's capacity to meet their assumed financial commitments. The situation of over-indebtedness occurs conceptually and temporally prior to insolvency, although that may be the cause of the latter and result in this legal state. Finally, insolvency (as an effective impossibility of regular performance of payment obligations) must also be distinguished from *arrears* and from *default* (as the materialisation of an actual situation of non-compliance with a concrete business relationship).[3]

2. *Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?*

Until recently, there was no specific definition of vulnerability either in consumer credit law or in the General Consumer Protection Act.[4] However the financial and economic crisis has triggered the Spanish Government to take into account situations of vulnerability with regard to consumers of financial services (specifically, individuals with mortgages who are experiencing serious difficulties in complying with their obligations and are at risk of losing their home) with an *ex post* approach; adopting certain extraordinary and urgent regulatory measures aimed at reinforcing the protection of the most vulnerable mortgagors from eviction.

Royal Decree-Law 6/2012 of 9 March, concerning urgent measures for the protection of individuals with mortgages without resources refers to those being in a "vulnerable situation" when all the following criteria are met:

- No member of the family unit receives any income derived from work or economic activity (i.e. all are unemployed).
- The mortgage payment is higher than 60% of the net income received by all the members of the family unit.
- None of the members of the family unit hold any other property or property rights to sufficient to satisfy the debt.
- The credit or loan is secured with a mortgage on the only house owned by the debtor, and has been granted for its acquisition.

Royal Decree Law 27/2012, of 15 November, on urgent measures to reinforce the protection of mortgagors, suspends evictions for two years for families at *special risk of exclusion*. It will apply to persons who are in a "situation of special vulnerability". To be considered in this situation (and, then, to be a member of "especially vulnerable groups") two kinds of requisites must be fulfilled.

The first, of a subjective nature, concerns the social groups which are in "particularly vulnerable situations": the family unit needs to fall under one of the following cases:

- large families,
- single parent, with two dependent children,
- with a child under three years of age,
- some members with declared disability (greater than 33%) of permanent dependency or disease permanently incapacitating with regards to work,
- an unemployed mortgage debtor without unemployment benefits,

3See Gutiérrez de Cabiedes, El Sobreendeudamiento doméstico..., p. 24.

4Consolidated Text of the General Act for the Protection of Consumers and Users, of 2007 (TR-LGDCU).

- living together with disabled or permanently dependent persons and united with the mortgage debtor or his or her spouse by blood relationship or family affinity to the third degree,
- or with a victim of gender violence.

Second, of an objective nature –additionally– related to the following economic circumstances:

- The total income of the members of the family unit does not exceed the threshold of three times the IPREM index.[5]
- In the four years prior to the demand (for the suspension of eviction), the family unit has suffered significant changes in their economic circumstances, in terms of "stress for accessing to housing" (household mortgage burden related to the family income has multiplied by at least 1.5% in that period of time).
- The mortgage payment exceeds 50% of the net family income.
- The mortgage loan secures the only home owned by the debtor (thus, excluding properties acquired in an auction proceeding by a third party).

Finally, Law 1/2013, of 14 May, on measures to reinforce protection of those with mortgages, debt restructuring and social rent ("Law 1/2013"), foresees a moratorium on evictions of those with mortgages at "special risk of social exclusion", practically in identical terms.

3. Is the term "poverty" or "low-income consumer" defined in the national legal order?

The term poverty is not defined with regard to consumers, but to citizens in general as the state of scarcity or lack of resources to meet basic human needs, which in Spanish legislation leads to the right to access certain social benefits and services.

The Spanish Statistical Office (INE) uses in its Living Conditions Survey (LCS) the concept of poverty threshold, which is a relative measure or indicator[6] (it is relative since it takes into account the situation of the population and depends on the distribution of income per consumption unit of people). The poverty threshold is set at 60% of median income per consumption unit of people. The value of the poverty level, expressed as total household income in euros, depends on the household size and the age of its members. As an illustrative value, according to information provided by the Survey of Living Conditions of 2012, the poverty threshold value of a single-person household was €7,182 per year. A person with an annual income per consumption unit below the value of the poverty threshold, depending on the type of household that applies to him or her, is considered to be at risk of poverty.

A quantitative threshold (or objective reference) for certain purposes is formed by the minimum wage: nowadays the IPREM index. "Low income" is defined in the same manner, related to those with mortgages at "special risk of social exclusion", "situation of special" or "particular vulnerability" (see above).

II. Numbers on over-indebtedness

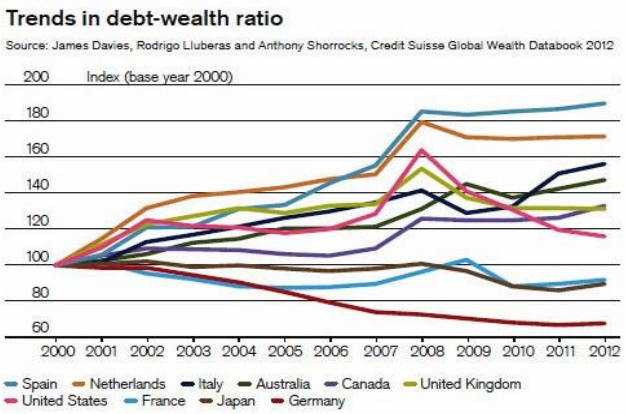
1. How many consumers are considered "indebted" in the country? (since 2000)

The last comprehensive study carried out by the Spanish Statistical Office on "Over-indebtedness and Financial exclusion" dates back to 2008, and reports that 16,921,800 households had some form of

5 Public Income Indicator for Multiple Effects, used as a reference for the concession of multiple subsidies, subventions, etc. which in 2012 reached 532 Euros per month

6 This indicator allows comparability with other countries of the European Union. It is part of the "Sustainable Development Indicators" and constitutes an essential element of reference for monitoring the National Action Plan for Social Inclusion (part of Community action in the fight against social exclusion). See Spanish Statistical Office, Wages, income, social cohesion, updated on 23 January 2014.

debt in Spain.[7] According to the Bank of Spain's "Survey of Household Finances", of the total households surveyed, 48.9% reported having no loans or credit, compared to the remaining 51.1% who have some form of loan.[8]



Source: The Debt of Nations[9]

a. How many consumers have mortgage debt?

There is no official statistics determining the exact number of mortgages existing in Spain. However we can estimate that the number of households with existing mortgages in Spain amounts to approximately 5 million (5,128,167) mortgaged homes (and 5.8 million taxpayers).[10]

Other official data that shows that 8.712.954 mortgages were concluded in Spain for the acquisition of housing in the last ten years;[11]and that the mortgage debt on principal residence is the most widespread type of loan.[12]

b. How many consumers have motor vehicle debt?

Around 2,656,720 households held a debt for the purchase of motor vehicle, according to latest Survey on Household Finances made by the Bank of Spain.[13]

c. How many consumers have other debt (credit card, general consumption)?

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7 Spanish Statistical Office, Life Conditions Survey, Special issue on Overindebtedness and Financial exclusion, 2008.

8 Banco de España, Encuesta Financiera de las Familias [Survey on Household Finances], 2010.

9 See Durden, T., The Debt of Nations, at http://www.zerohedge.com/news/2013-06-04/debt-nations.

10 To reach this conclusion, factors that must be taken into consideration include firstly the number of households in Spain. Currently, there is no housing census, nor any classification of properties according to their use (statistics forthcoming). Determining the number of households with a mortgage is complex given that the latest statistics available from the Spanish Statistical Office place the number of households with a mortgage at the 29.9 % of all households in Spain. Based on the validity of on a report by the defunct Ministry of Housing issued in 2007, which held a screening of 17.1 million households in 2013 for a population of 46.4 million people, we can estimate that there are 5,128,167 mortgaged homes in the country.

If we compare, for instance, the number of mortgages that exercise tax deduction for house purchase (primary residence), we can observe that there are 5.8 million taxpayers applying this deduction (2010 income tax data). Therefore, we can assume that the above calculation is reasonably accurate, given that it is possible for two people to deduct the same mortgage loan and that the individual income tax return is the usual formula when both spouses work,: see http://www.elblogsalmon.com/mercados-financieros/cuantas-hipotecas-se-pueden-favorecer-de-la-iniciativa-legislativa-popular-de-dacion-en-pago.

11Spanish Statistical Office, Financial and monetary statistics. Data from 2003 to 2012. See http://www.ine.es/inebmenu/mnu_financie.htm.

12 Spanish Statistical Office, Life Conditions Survey, 2012.

13 Banco de España, Encuesta Financiera de las Familias [SurveyonHouseholdFinances], 2010.

The percentage of Spanish households with outstanding debts (at the time of completion of the Survey on Household Finances) to finance general consumption (non-real estate debt) is 33.4%.[14] Out of the total, 23.1% corresponds to personal credit, 7.3% to credit card debt and 3% to other debts secured by real estate (but not for purchase of real estate). Such debt represents 15.8% of the total debt of Spanish households (compared to 84.2% belonging to real estate). Estimated calculations of consumer organizations stand at about 6,500,000 million consumers who have credit card debt in Spain.[15]

d. What percentage of those "indebted" consumers / households(a, b, c) is:

i. Single / married

ii. With / without children?

iii. With / without work?

iv. Retired?

v. Low-income consumers?

The data gathered by the Spanish Stats (of those asked) relates to the employment status of the head of the household (classifications are made in relation to different criteria: i.e. nationality, region, sex, home size and educational level). It shows that the percentage of indebted households in which its head is: an employee (68.3%), self-employed (63.9%), retired, (22.2 %), and unemployed (36.7%). In addition, indebted households with low incomes or those in which any member of the household is working are those with the highest median debt burden ratios (with highest levels of financial pressure); but they represent a small percentage of the total households.[16] There is no data about the other types of statistical disaggregation (e.g. single or married, with or without children).

2. How many consumers/households are considered "over-indebted" in the country? (since 2000)

According to data from the Bank of Spain, in 2007 (before the crisis) nearly one in five households could be considered as being over-indebted.[17]According to data from the Spanish Statistical Office, in 2013, 16.9% of Spanish households reported "serious difficulties" to meet their expenses[18].Meanwhile, 40.9% of households were not able to handle unforeseen expenses.

a. How many individual consumers/households are behind with the repayment of (up to 3 months and more than 3 months):

i. General consumption loans

ii. Motor vehicle loans

iii. Student loans

iv. Credit card debt

v. Mortgages / housing loans

vi. Interests

There is no data about this kind of statistical disaggregation. However, we know that 9.2% of households face late payments when paying expenses related to the main residence (mortgage loan,

14 Banco de España, Encuesta Financiera de las Familias [SurveyonHouseholdFinances], 2010.

15 Estimated calculations provided by Adicae, Spanish organization of banking services.

16 Banco de España, Encuesta Financiera de las Familias [Survey on Household Finances], 2010.

17 Banco de España, Encuesta Financiera de las Familias [Survey on Household Finances], 2010.

18 Spanish Statistical Office, Life Conditions Survey, 2013.

rents, energy bills, gas, electricity, etc.).[19] The last specific study carried out on the over-indebtedness of Spanish consumers showed that in 2009, 7.2% of households where behind with the repayment of general debts related to the main residence, and 3.2% faced delays in the repayment of deferred payments and other loans not related to the main residence.[20]

b. How many individual consumers / households have initiated bankruptcy proceedings?

The initiation of bankruptcy proceedings of individual consumers is not a common practice in Spain (see below, section VI,§1, paragraphs a) and d)). As a result, according to the Spanish Statistical Office, only 726 consumers initiated bankruptcy proceedings in 2013.[21]

The following chart shows the evolution of consumer bankruptcy proceedings (and its reduced amount in absolute terms), in the main years of the financial crisis:

Source: Spanish Statistical Office

c. How high is the average amount of outstanding debt?

The average amounts to €36,000.[22]

d. What percentage of those "over-indebted" consumers/households(a and b)is:

i. Single / married?

ii. With / without children?

iii. With / without work?

iv. Retired?

v. Low-income consumers?

There is no data available about this kind of statistical disaggregation, nor can it be obtained with the necessary level of accuracy. The data gathered by the Spanish Statistical Office is related to risk of poverty and classifications are made in relation to different criteria such as nationality, region, sex, home size and educational level. A special issue on *Over-indebtedness and Financial Exclusion* by the Spanish Statistical Office is forthcoming in 2014.

III. Numbers on evictions

1. How many evictions have there been per year since 2000 (or later if earlier data not available)?

There are no consistent figures on evictions in Spain or its typology; for instance, there is no clear distinction of the number of evictions of residential properties and non-residential properties.[23]

19 Spanish Statistical Office, Life Conditions Survey, 2013.

20 Spanish Statistical Office, Household and Financial Statistics, 2010.

21 Spanish Statistical Office, Bankruptcy Proceedings Statistics, 2014.

22 Banco de España, Encuesta Financiera de las Familias [Survey on Household Finances], 2010.

According to the available data provided by the Spanish General Council of the Judiciary, there have been a total of 485,828 evictions since 2007.[24]

Foreclosures culminating in evictions			
07-T1	5,688	10-T2	24,533
07-T2	5,935	10-T3	19,358
07-T3	5,484	10-T4	22,148
07-T4	8,836	11-T1	21,737
08-T1	11,050	11-T2	20,505
08-T2	12,938	11-T3	14,861
08-T3	13,487	11-T4	20,751
08-T4	21,211	12-T1	24,699
09-T1	23,433	12-T2	23,342
09-T2	23,704	12-T3	19,238
09-T3	19,241	12-T4	24,343
09-T4	26,941	13-T1	21,272
10-T1	27,597	13-T2	20,323

Source: General Council of the Judiciary

One can observe that, as a result of the crisis in 2008, in just one year, the number of foreclosures culminating in evictions doubled and that this trend has continued to date standing at around 20,000 evictions per term (3 months).

According to this data, there were 91,622 judicial foreclosures in 2012; representing around 517 per day.[25] More specifically, the Bank of Spain and the filtered data from financial institutions that managed more than 85% of mortgage lending reported that in 2012 there were 32,490 foreclosures of home residences out of which 14,110 were given as payment for outstanding debt (43% of total) and another 4,215 were voluntary surrenders. When the judicial commission tried to execute the eviction, 2,405 homes were still occupied and police intervention was required in 355 cases.[26]

Therefore, although data provided by notaries and registrars are extraordinarily high, it is also important to point that this data includes evictions of local non-built properties, second homes, etc.

2. *How many evictions took place because of:*
   a. *Unpaid mortgage instalments?*
   b. *Unpaid monthly rent?*

(Contd.)

23 This issue is even highlighted by a recent report of the General Council of the Judiciary: Consejo General del Poder Judicial, «Una aproximación a la conciliación de los datos sobre ejecuciones y desahucios», Boletín Información Estadística, n. 35, junio 2013 ["An approach to the Reconciliation of Data on Foreclosures and Evictions"], which attempts to solve precisely this lack of clarity and to provide consistent figures in this regard.

24 Consejo General del Poder Judicial, Datos sobre el efecto de la crisis en los órganos judiciales. Desde 2007 hasta el tercer cuatrimestre de 2013 [Data on the effect of the crisis in the Judiciary. From 2007 to the third quarter of 2013], available at

http://www.poderjudicial.es/cgpj/es/Poder_Judicial/Sala_de_Prensa/Notas_de_prensa/Datos_sobre_el_efecto_de_la_crisis_en_los_organos_judiciales_en_el_tercer_trimestre_de_2013

25 General Council of the Judiciary, Data on the effect of the crisis in the Judiciary. Third quarter 2013, available at

http://www.poderjudicial.es/cgpj/es/Temas/Estadistica_Judicial/Informes_estadisticos/Informes_periodicos/ci.Datos_sobre_el_efecto_de_la_crisis_en_los_organos_judiciales___Actualizado_al_tercer_trimestre_de_2013.formato3.

26 Bank of Spain, 'Nota informativa sobre la presentación de una nueva estadística de procesos de ejecución hipotecaria sobre viviendas', Available at

http://www.bde.es/f/webbde/GAP/Secciones/SalaPrensa/NotasInformativas/Briefing_notes/es/notabe10-05-13.pdf.

As aforementioned, there are no consolidated figures of the amount of evictions from neither unpaid mortgage instalments nor those which take place as a result of unpaid rent.[27] For its part, the GCJ reported that in 2012, 17,716 *judicial proceedings* related to unpaid monthly rent.[28]However, the GCJ does not specify whether those figures culminated in evictions or not.

3. Who are the persons affected (percentage of young people, families, retirees, unemployed, level of education, low-income consumers)?

Typically affected by this situation are families in which one or both parents have lost their job, sometimes with every single member of the family unemployed and with no income at all. Immigrants who moved to Spain in the boom years were the first to lose their jobs in the downturn, and have been the most severely affected so far, although there are also native Spanish in similar circumstances.[29] Less numerous groups are retired people and young people.

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

1. Is the CCD 2008/48 implemented into national law?

Yes. The Spanish Law on Consumer Credit Contracts (Law 16/2011, of 24 June) implemented a standard transposition of Directive 2008/48. It entered into force in September 2011.

2. Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?

Law 16/2011on Consumer Credit Agreements does not apply to mortgages. Article 3 a) in of the Spanish text, in line with the Directive in Article 2(2) a), explicitly excludes "credit agreements which are secured by a real estate mortgage". By so doing, they remain regulated by Law 2/2009, by the general mortgage regulation and by specific banking regulations.[30] However, Spanish Law goes beyond the Directive in other aspects. Since the transposed Directive is a maximum harmonization measure, but its scope only affects to "certain aspects" of consumer credit agreements, the Spanish Law on Consumer Credit maintains those provisions of the former national Law that provide higher protection to credit consumers – although they were not required by EU's legislation.

3. With regard to the Mortgage Credit Directive, will there have to be an adjustment of national law? What are the changes in particular?

Most of the changes that may be derived from the Directive had already been implemented in Spain by the Law 1/2013, passed as a consequence of *Aziz* ruling and as a result of social pressure.[31]

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27 Nonetheless, it is envisaged that the Spanish Statistical Office begins publishing a new quarterly statistics of foreclosures and evictions that take it into account.

28 Data available at http://www.ine.es/jaxi/menu.do?type=pcaxis&path=/t18/p464&file=inebase.

29 The New York Times, "In Spain, Homes Are Taken but Debt Stays", The New York Times, New York edition, October 28, 2010, page A1.

30 Previously passed were the Order EHA/2899/2011, of October 28th, on banking services transparency and customer protection) and the Circular of the Bank of Spain 5/2012 of June 27, on transparency in banking services and responsibility in lending.

31 Large demonstrations, organized by the 'Plataforma de Afectados por la Hipoteca' ('Platform for Mortgage Victims'), were held all over Spain in 2012 and 2013, and a citizens' legal initiative ("Iniciativa Legislativa Popular": ILP) was submitted in the Spanish lower house of Parliament with the support of 1.402.854 signatures. The government and opposition parties were forced to submit their respective draft law on this matter in the parliamentary proceedings of this "citizens Legislative Initiative". The outcome of these proceedings was the above mentioned Law 1/2013.

4. How is the national legal framework with regard to the UCT 93/13?

Directive 93/13 was the legal text whose implementation took the longest (there was a delay of some 40 months). It was transposed into the Spanish legal system by the Standard Contract Terms Act (Law 7/1998). The assessment of unfairness refers to B2C standard terms. Further, in some aspects the Spanish legislation (now also reflected in the Consolidated Text of the General Act for the Protection of Consumers and Users, of 2007: TR-LGDCU) has gone even beyond the provisions of the Directive, for instance in relation to the black list of unfair terms.

However, the Court of Justice of the European Union (CJEU) ruled that (Case *Commission v Spain*) Spain failed to fulfil its obligations with regards to transposing into the national legal system Articles 5 and 6(2) of the Directive.[32] In its judgment of 14 June 2012 in Case *Banco Español de Crédito (Banesto)*,[33] the CJEU found that Spain had not correctly transposed Article 6(1) of the Unfair Contract Terms Directive as far as the Spanish domestic legislation empowered the national court to modify the content of unfair terms in contracts in order to integrate the invalid part into the contract under the principle of objective good faith (integration of the contract). The Court considered that this practice could jeopardise the achievement of the long-term goal referred to in Article 7 of the Directive, as long as it might contribute to eliminate the deterrent effect it has on professionals to make use of unfair terms.

Moreover, the lack of formal implementation of article 4.2 of the Directive 93/13/EEC produced a strong legal uncertainty in the Spanish case-law, as for determining whether a non-negotiated term which defines the «main subject matter» of the contract (and even the «adequacy» between price as against goods or services in exchange) can be declared void as an unfair term, provided that these terms are in plain intelligible language.[34]

The *Caja Madrid* judgment delivered June 2010 stated that Member States, when faced with the transposition of that Article, may allow a full jurisdictional control of all kind of terms, including the so-called "core terms", since this represents an increase in the level of consumer protection.

The potential interpretation of the case *Caja Madrid v Ausbanc* should be borne in mind[35] in combination with the cases of *Banco Español de Crédito* and *Aziz*.[36] Once the nullity of the loan is declared, it is also possible to annul the mortgage given its accessory character in relation to the principal contract. Nobody can deny the impact this would have on the Spanish mortgage market and, according to some, in the mortgage itself as an institution.

The Supreme Court judgment of 9 May 2013 (judgment in plenary session of the Spanish Supreme Court on the "floor terms" in mortgage credits) settled the issue in national law. The ruling, in view of the "risks" for the mortgage market and, thereby, for the stability and "reliability" of the Spanish economic system and despite certain claims of the Judgment on the case *Caja Madrid v Ausbanc*, states that considering Article 4(2) of Directive 93/13, the Spanish legal system does not allow the assessment of unfairness of those terms that define the main subject of the contract (including price), unless they are not displayed to the consumer in a transparent way.

Finally, with the recent enactment of Law 3/2014 of 27 March, transposing Directive 2011/83/EU on Consumer Rights (including the amendment of Directive 93/13/EEC), the Spanish legislature has developed a (minor) reform of the TR-LGDCU, in order to adapt its content to the Consumer Rights

32 Case C–70/03 *Commission of the European Communities v Kingdom of Spain* [2004] ECR I-07999.

33 Case C-618/10 *Banco Español de Crédito SA v Joaquín Calderón Camino*; not reported yet.

34 Cámara, S., 'El control de cláusulas abusivas sobre el precio: de la STJUE 3 junio 2010 (Caja Madrid) a la STS 9 mayo 2013 sobre cláusulas suelo', Revista CESCO de Derecho del Consumo, no. 6/2013, pp. 98-115.

35 Case C-484/08 *Caja de Ahorros y Monte de Piedad de Madrid v Asociación de Usuarios de Servicios Bancarios (Ausbanc)* [2010] ECR I-04785.

36 Case C-415/11 *Mohamed Aziz v Caixa d´Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa)*; not reported yet.

Directive and its claim to full harmonization, and also to comply with the Judgment of the CJEU on the *BancoEspañol de Crédito* case so that the contract will remain binding on the parties, provided that it can survive without the terms that were found "unfair".

V. Enforcement of consumer credit contracts

1. What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?

The main maxim *pacta sunt servanda* is found in the Spanish legal system in Article 1091 of the Spanish Civil Code: 'Obligations arising from contracts have force of law between the contracting parties, and must be fulfilled'. Default on any payment actually constitutes a breach of contract and may lead to its termination. As such, the lender is granted legal standing to begin foreclosure proceedings; that is a special enforcement procedure where takes place the public auction of the mortgaged property. Furthermore, the lender is entitled to sue in an ordinary enforcement proceeding for the rest of the debt that could not be obtained through the sale of the mortgaged property. In this procedure, other debtor's assets are able to be seized and sold at public auction.

The rough social and economic situation and the struggling conditions for many families are also significant problems. In this regard, there is a remarkable social, political and legal proposal and debate on the introduction in Spain of the "*dación en pago*" (*datio in solutum*). This institution means that borrowers who have given immovable property - usually their homes - to the lender as a mortgage can be released from their obligations resulting from the loan if the mortgaged property is given to the mortgage holder through the judicial process. Such an adjudication takes place when, in the course of the foreclosure proceedings, the sale by public auction of the immovable property given as a guarantee is not completed due to a lack of bidders or third parties interested. In this case, according to Spanish Law, the creditor may request the court to adjudicate the mortgaged property to him; but that adjudication does not put an end to the obligations secured by the mortgage. On the contrary, the creditor may continue to claim from the debtor the part of the debt not satisfied after the adjudication in an ordinary enforcement proceeding (even after the creditor has sold the adjudicated immovable property to a third party for a higher value). According to Article 105 of Mortgage Law ("Ley Hipotecaria", hereinafter LH), passed by the Decree of 8 February 1946:

"The mortgage . . . will not alter the unlimited personal liability of the debtor provided in art. 1911 of the Civil Code". And, therefore, neither does the foreclosure: the creditor may continue collecting the "outstanding debt"(the amount that remains unpaid and which it is considered that still owes) from the debtor's remaining and even future assets in the aforementioned execution (enforcement) proceeding. This is what art. 1911 of Civil Code establishes in a categorical and solemn way: "The debtor is liable for the performance of his obligations with all his assets, present and future".

This scheme favoured a praxis by which the creditor (normally, a bank) was incentivised to transfer the property - which has been acquired by the same creditor (i.e. appraisal services linked or dependent on the bank) at a price that is well below the assessed value of the mortgaged property- to a third party; while still claiming the amount of the unsatisfied debt from the debtors. This practice is very disadvantageous for debtors (usually unemployed or retired people, struggling and vulnerable families), who have lost their house precisely because of not having either income or assets.

Spanish mortgage law has enabled the extrajudicial sale of the property for the enforcement of the mortgage by the creditor and did not foresee any limit to the price of the transaction.37 The mortgaged

37 Article 129 of the Spanish Mortgage law (before the amendments introduced by the Royal Decree-Law 6/2012, of 9 March, concerning urgent measures for the protection of those with mortgages without resources that is analysed subsequently).

properties were publicly auctioned, and the real estate agencies from the creditor banks themselves were the ones who attended these auctions being the properties awarded at much reduced prices. In the absence of any limit to the auction price, the law allows them to acquire the property for 50% of the public auction if it is forfeited, which occurs in the 90% of cases.[38]

This situation sparked strong public controversy. It is noteworthy that some judicial decisions from lower courts have attempted to curb this practice by considering the conduct of the banks as an "abuse of rights," "anti-social exercise," or "an excess of authority" (terms which are referred to in Article 7(2) Civil Code)[39] regarding the rights derived from the mortgage;[40] and, on this basis, some Courts have denied the right of the creditor bank to pursue the collection of the outstanding amount of the mortgage on the remaining assets of the mortgagor.

In particular, several decisions of the Provincial Court of Navarra, mainly the decision of 17 December 2010 (of extremely significant social relevance), in which the bank (BBVA, one of the main banks in Spain) was obliged to accept this solution of "*datio in solutum*" to extinguish and cancel the debt. Those decisions were followed by others, such as those of the Provincial Court of Girona, 16 September 2011 and that of the Court of First Instance of Lleida No. 5, 9 December 2011. The Court of Appeal considered that giving the house to the bank with its value was enough to cover the debt, and so discharged it; considering, moreover, that if the bank granted the loan it was because the house had a higher value than the credit.

Jurisprudence and scholarship has also remarked that judgments should reflect the current economic and social reality, one of the main criteria of legal interpretation established by Article 3.1 of the Spanish Civil Code: "The law will be interpreted (...) according to the social reality at the time they should be applied". Furthermore, the current social and economic outlook has little to do with the one that existed when the contract was signed. Some of the decisions even add this certain systemic or socio-political considerations to their reasoning.[41]

However, the Court of Appeal of Navarra (in which there was a divided opinion and debate among the members of the bench) soon issued further different and opposite Orders, first and principally, in 4 February 2011. This Order stated that the debt attached to the mortgage was not cancelled by acquiring the house through an auction, considering that the value of the property was lower than the debt. This later resolution is significantly different and applied the principle of the Spanish Civil Code

38 Sempere, J. 'El escándalo de la vivienda', 14 October 2010, Diario Público (SpanishDailyJournal)

39 Article 7.2 CC sets up that "[t]he law does not support abuse of rights or antisocial exercise thereof. Any act or omission which, as a result of the author's intention, its purpose or the circumstances in which it is performed manifestly exceeds the normal limits to exercise a right, with damage to a third party, shall give rise to the corresponding compensation and the adoption of judicial or administrative measures preventing persistence in such abuse".

40 The Court of First Instance of Lleida, December 29, 2011, states: "we must not forget that when the Bank granted the loan, it valued the property or estate at €219,242.55, and now intends to incorporate it into their assets for a value of €109,621.28, and to continue the enforcement process on the other debtors assets". It considers that the „*venire contra factum proprium*" doctrine, analogue to the estoppel doctrine, applies here. If the bank, the dominant party in the contract of adhesion with the borrower, appraised the mortgaged property at a certain amount, it cannot then incorporate as its own the mortgaged property without giving it the value that [the creditor bank] itself set (and fixed by the parties). The incorporation of this patrimonial asset at a lower value to which the party has acknowledged, intending to continue the enforcement process, presumes an *abuse of rights* by the creditor, and allows an *unjust enrichment* of the Bank. Further the purpose of foreclosure is to obtain for the creditor, with the auction of the property, the collection of the outstanding debt, but not to obtain an unjust benefit.

41 So does, for example, the aforementioned Order of Court of First Instance of Lleida No. 5, 29 December 2011, wondering: "is it fair that the debtor suffers all the consequences of this fall? Would it not be fairer that the financial institutions also bear part of this decline? Economists are unanimous in considering that the real estate value losses have been caused by the financial institutions themselves with their mismanagement of the financial system. Hence, if the laws should be interpreted according to the reality at the time when they are applied (article 3 of the Spanish Civil Code) . . . [it] is not acceptable that the stronger party in the mortgage loan contract obtains an unjustified benefit with the further execution at the expense of the debtor".

which considers that the debtor will have to pay all debts with his current or future assets, and that Judges shall fulfil the law accordingly.

Finally, the Supreme Court rejected that original approach ruling that the creditor's performance does not constitute an abuse of rights when claiming the enforcement of their rights according to the powers granted by the law, and if the foreclosure proceeding has been followed according to the legal procedure by the mortgagee. In addition, the Court holds that preventing the creditor from exercising those rights would undermine the general confidence in the performance of contractual obligations.[42]

In the same vein, the Constitutional Court, in its Decision 113/2011 of 17 August 2011, censured such a judicial approach. The judges criticised the earlier decision for using the rules for foreclosure proceedings, exceeding their interpretative role and the existing legal framework, which, in a system of law such as that of Spain, can only be modified by the legislature. The Constitutional Court held that foreclosure proceedings do not infringe on the principles of effective judicial protection and procedural fairness between the parties, and that the absence of procedural opposition within the mortgage enforcement procedure does not cause inability to defend given the possibility of initiating a subsequent assessment procedure (declaratory proceedings).[43]

This is the reason why the legislature itself decided to intervene in order to try to remedy or, at least to relieve the severity of the above-mentioned social-economic situation. Although these legal reforms carried out in Spain are widely considered as not being adequate to relieve the consumer's burden. Several opposition parliamentary parties have been pushing for amendments to the country's foreclosure laws, including the possibility for allowing "lieu of payment" (i.e. the mortgage defaulters to settle their debts with the bank by recovering the property). But the Government (first, the Socialist Cabinet of José Luis Rodríguez Zapatero, and later on, the Popular Party of Mariano Rajoy) has opposed such a major change in mortgage credit laws. Government officials say the Spanish system of personal guarantees prevented its banks from the turmoil experienced in the United States.

2. What are the requirements to initiate enforcement procedures against the consumer?

Enforcement action must be based on an instrument which is enforceable, according to Article 517(1) Spanish Civil Procedure Act (CPA) and Article 517(2)CPA. Such enforceable titles are: a definitive conviction court decision; arbitration awards or resolutions and mediation agreements, the latter of which shall be made public by means of a public deed in accordance with the Mediation Act on Civil and Commercial Matters; court rulings which approve court settlements and agreements achieved in the proceedings; public instruments; commercial agreements signed by the parties and by a Notary Public.

In the field of foreclosure, the existence of failure (default in payment) is required to initiate the enforcement procedure against the borrower. The lender must only show that the mortgage credit agreement and the debt exist.

3. What are the steps of such enforcement procedure?

- Enforcement Claim

42 Mainly in the judgments of Supreme Court, of 16 February 2006 (RJ 2006, 710) and 25 September 2008 (RJ 2008, 5570) holding that to exercise the rights conferred by law in order to obtain "admissible economic benefits" in those transactions is not per se an abusive. In this regard, there is case law both in favor and against this doctrine by the different Spanish Courts of Appeals (*Audiencias Provinciales*), 5th legal basis.

43 Order of the Constitutional Court 113/2011, of 19 July.

The enforcement procedure[44] starts with a writ of demand or statement of claim. This claim must specify a number of essential elements: the enforcement sought, the person or persons against whom the decision is to be enforced and their circumstances. Furthermore it must be accompanied by the corresponding "enforceable instrument" together with other relevant documents (i.e. information about the assets of the debtor) pursuant to Article 549 of the Civil Procedure Act. In Spain enforcement is always carried out by the Court: thus, the demand must be filed usually before the competent Courts of First Instance.

- Decision: granting the enforcement ("order of execution")

If the enforcement application meets the requirements, enforcement will be granted by the judge, determining the amount to be seized, the persons concerned and the enforcement measures. If the enforcement is for payment of monetary obligations, the debtor's property shall be seized. As such the court shall order a public sale (auction). In order to guarantee the effectiveness of enforcement and attachment, the law provides for certain measures depending on the type of asset:[45] enforcement measures remain in force until enforcement is complete.

- Opposition

Appeal is not possible against specific measures laid down in the decision granting enforcement, but the debtor may oppose the adoption of the order of execution or of specific enforcement measures. In this case, the debtor may initiate appeal proceedings against the court's dismissal within a period of five days. Initiation of appeal proceedings does not suspend enforcement of the measures granted. As for the grounds of opposition, see next question.

- Collection Proceedings

This stage of proceedings consists of the *public sale* of the attached property, in order to pay the judgment creditor (or the *direct adjudication* of money or of the property attached; or *payment*). Its steps are the appraisal of property, the advertisement of the sale, the sale itself, award of property, possible administration and settlement of any outstanding encumbrances against the property.

- Termination

Until the creditor has been entirely paid his principal and interests in full, and the costs of the proceeding have been covered, the proceeds from the sale may not be used for any other purpose (the debtor is liable for all costs occasioned by enforcement proceedings). Consequently the enforcement process terminates only when the whole debt, principal, interests and costs are fully paid.

4. Can the consumer raise substantive objections against enforcement?

Yes. The CPA provides the possibility for the debtor to oppose the decision of enforcement measures. In the case of judgments, as there has been a previous process during which there were extensive opportunities for debate, there are fewer possibilities of opposition. In addition, in mortgage enforcement proceedings, they have traditionally been even much more restricted in terms of possibilities of opposition, because of its alleged "special nature", until the recent reform carried out in 2013.

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44 See Cremades& Gutiérrez de Cabiedes, Litigating in Spain: considerations for foreign practitioners, including international judicial assistance, enforcement of foreign judgments, bankruptcy, arbitration, and other civil proceedings, Kluwer-La Ley, Madrid; European Commission, „Enforcement of judgements – Spain", in

http://ec.europa.eu/civiljustice/enforce_judgement/enforce_judgement_spa_en.htm .

45 In the case of immovable property or other assets that can be entered in a register, the court may, at the request of the party applying for enforcement, order a preventive annotation of seizure in the corresponding public register (usually the Property Register, which is the one for immovable property).

In other cases, the following measures may be granted: money: confiscation; current accounts: order to the bank to block the accounts; salaries: order to the payer to withhold part of the payment; interests, proceeds and revenue: withholding by the payer, receivership and judicial confiscation; other movable property: confiscation.

a. Which ones?

The debtor may oppose the enforcement either on the basis of procedural shortcomings or substantive objections about the legal relationship in question.

- Procedural reasons (applicable to all enforcement instruments) :
  - The debtor does not have the capacity or representation required;
  - Lack of capacity or representation on the part of the plaintiff or his inability to prove the capacity or representation required;
  - Absolute invalidity of the enforcement granted because it does not contain the judgment or arbitration decision finding against the defendant, because the document produced does not comply with legal requirements for enforceability, or because of a violation, when the enforcement was granted, of the rules governing the proceedings to be followed before granting an enforcement measure;
  - If the enforcement instrument was an arbitration award that was not placed on record by a notary, the lack of authenticity of this decision.
- material grounds:

If the enforcement instrument is lato sensu "judicial" (court decision, judgment, arbitration award, settlement) the debtor may, within ten days following the notification of the act in which enforcement is granted, oppose this in writing on one of the following grounds:

- Payment or compliance, with what is ordered in the judgment, which will have to be established by documents;
- Lapse of the enforcement action;
- Agreements and settlements that were reached to avoid enforcement, if such agreement is recorded in a public document.

However if the enforcement instrument is different (non-judicial) there are more grounds for opposition, including the following:

- Offsetting of a payable claim based on a document that is enforceable;
- Plus petitio or excess in the evaluation of debts in cash;
- Limitation and lapsing;
- Acquittal, respite, or an agreement or promise not to sue, recorded in documents.
- A settlement, provided that it is set down in a public document;

b. What is the legal effect of such objections?

Procedural effect

- In the first Payment, documentary evidence of which must be provided;

  cases (opposition against enforcement of *judicial* instruments), the opposition does not suspend enforcement. In the second (opposition against enforcement of *no-judicial* instruments) is formulated in these cases, enforcement is suspended.

Effect of substantive objections

Where the substantive opposition succeeds, the enforcement order shall have no effect, and the enforcement proceeding will be terminated. If it succeeds in its entirety, the applicant should pay the opposition fees paid by each of the opponents.

5. Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?

Ordinarily, it is not possible to make adjustments of contractual terms without the consent of the two parties (Article 1256 of Spanish Civil Code). But at the same time, the Spanish Civil Code takes into account the institutions of "*force majeure*" and "*fortuitous event*" (both together and individually), generally and implicitly defined by Article 1105 CC: "Outside the cases expressly mentioned in the law, and those in which the obligation should require it, no one shall be liable for events which cannot be foreseen or which, being foreseen, should be inevitable".

a. How is the term "unforeseen/unforeseeable events" defined?

These terms are used expressly in the Spanish Civil Code such as in Article 1575[46] which talks about "unforeseen fortuitous events", describing them shortly after as "extraordinary and unaccustomed events, which the contracting parties should have been unable to foresee reasonably". Consequently, they must be understood as supervening exceptional circumstances that are outside the control of the parties which makes impossible performance of the contract.

b. If adjustment is possible, what are its legal effects?

Force majeure is set as a ground for exclusion of liability of a party for non-performance of the contract which usually relieves one or both parties to a contract of their contractual obligations (Article 1105 CC).

6. Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?

The key difference between the *force majeure* and the frustration of contract ("rebus sic stantibus") clause is that, in the former, performance (the fulfilment of the contract) has become impossible whereas in the latter it is excessively burdensome (as a result of unforeseen circumstances).

The Spanish Civil Code, which enshrines the principle of *pacta sunt servanda* (Article 1254 CC), did not consider the institution of reviewing or cancelling a contract on the base of the alteration of circumstances. However, the Spanish Supreme Court started to apply the *rebus sic stantibus* doctrine after the Spanish Civil War (namely in the 1940s, albeit in a restrictive manner), which is similar in nature to the frustration of contract or of purpose. The Court has continued applying this principle based on equity in such cases where a supervening extraordinary alteration of the circumstances (related to the time of performance of the contract with regard to the existing ones at the time of its conclusion) is given, producing an outrageous imbalance between the parties or hardship, not existing any other legal means to compensate for this imbalance.

Some scholars and Spanish judges (in court decisions and in a Report written by various judges and backed by an assembly of Spanish judges, although not supported by the General Council of the Judiciary) have proposed and called for the application of the principle *rebus sic stantibus* to mortgage loans, in order to be able to request the modification of the contract terms or the termination of contracts, according to each particular case. Thus, that formula would be applied in the event of severe alteration of the circumstances in which mortgage loans were signed compared to a subsequent situation, for instance, due to the current economic crisis. However, the Spanish Supreme Court and many appeal courts (provincial High Courts) have so far declared that the economic performance of a country and the situation of global economic crisis or the crisis of a specific industry cannot imply a general justification for the breach of the contractual obligations.[47]

46 This Article is a special provision for leases of rural properties.

47 See the Supreme Court's decision of 27 April, 2012 (RJ 2012\4714), which states that "the economic transformation of a country, provoked, among other reasons, by such evolution, cannot be used as a basis for the fulfilment of the requirements set by the case law to describe the existence of a disproportionate imbalance based on unforeseen circumstances, since the referred circumstances cannot have such a classification". A vast number of decisions from provincial High Courts had rejected the application of the principle rebus sic stantibus in the last years, concerning the current economic crisis, primarily in property purchases.

The Spanish Supreme Court, in its decision dated 17 January 2013[48], defines the criteria for the application of the *rebus sic stantibus* principle and analyses the predictability of the current economic crisis for its consideration as a factor which could lead to a change in the circumstances when applying the principle. The Court reviewed to a certain extent its prior doctrine, facilitating the application of the principle with a greater flexibility. Within its exceptional nature, the decision admits that a situation of economic crisis might imply an extraordinary alteration of circumstances.

"A situation of economic recession as the current one, with prolonged and deep effects, may be regarded, if the contract had been concluded before the external manifestation of the crisis, as an extraordinary manifestation of the circumstances, capable of originating, provided that other requirements are met (…) an exorbitant disproportion and out of all calculation of the performance of the parties"

The Court also refers to the circumstances that may lead to the application of the principle. Among those circumstances mentioned *ad exemplum* (the decision uses the expression "such as"), it takes into account:

"the economic situation of the buyer at the time of execution of the contract and the time of having to pay the outstanding part of the price that she was expected to finance; the actual degree of impossibility of funding and specific causes added to the general economic crisis".[49]

This substantial and supervening alteration of the circumstances, which is closely related to ("passive") over-indebtedness has been also addressed in a more or less indirect way, in the most recent regulatory provisions passed by Spanish Government: RD 27/2012 and Law 1/2013. These new rules are mainly aimed at acknowledging the need for reinforcing the protection of debtors who, as a result of exceptional circumstances, have suffered a "significant alteration of their economic circumstances". Pursuant to the Law 1/2013, this situation occurs when the effort involved in the mortgage burden on family income has increased 1.5 times at least. In such cases, the law establishes the application of the Code of Good Practices which provides complementary as well as substitutive measures aimed at debt restructuring and even, under fulfilment of the requirements, debt relief by the takeover of the property by the creditor (see also § I.1 and 2; and § VI.2)

7. Do the banks use private companies that deal with the recovery of debts with the result that legislation on consumer protection doesn't apply anymore?

In Spain, the use of specialised firms engaged in the recovery of debts is common practice. This activity can be based on an assignment of credit (the debt has been assigned to or purchased by the debt recovery company, and subsequently it becomes the new creditor) or on a simple agency or mandate contract for debt management (and so being the company a third party merely authorised to collect the debt). However, it makes no difference to the consumer and the protection of their interests that the original creditor (provider of the credit or service) uses another company to deal with the recovery of debt since even in case of credit assignment, pursuant to assignment of rights and credit regulations,[50] the same objections that could be raised against the original creditor can be raised against to new creditor.

48 Judgment of Supreme Court n. 820/2013, January 17th 2013, available at

http://portaljuridico.lexnova.es/jurisprudencia/JURIDICO/193741/sentencia-ts-820-2013-sala-1-de-17-de-enero-compraventa-de-vivienda-financiacion-impago.

49 The decision considers other nearby criteria: "the destination of the house, purchased as a principal residence or, on the contrary, as a second residence (...); the contractual allocation of risk of not having funding and the level of promised cooperation by the seller for purchase, distinguishing between contractors who are professionals of real estate and those who are not; (…), and, if being necessary also to assess, where appropriate, the conditions imposed by the banks to provide financing or, finally, the chances of negotiating payment terms with the seller (...)".

50 According to Articles 1526 et seq. of the Spanish Civil Code and case law on this matter.

These companies are notorious for their unfair (and even aggressive) practices for the recovery of debts. In this regard, there is a lack of specific regulation of this activity and of a standard license regarding the companies who are able to perform debt recovery activities (based on an assessment of whether they have the appropriate knowledge, skills and fair business practices and procedures to hold a license). Consequently, the Spanish Office of Data Protection has played an important role in the investigation of citizen's complaints and in the prosecution for breaching Data protection legislation (data transfer, unjustified inclusion in defaulters registries etc.). In addition, Courts have ruled against these companies for carrying out practices which threaten the dignity of those who see their privacy invaded or who are coerced as a result of these practices.

This notwithstanding, the subrogation of the creditor's rights has not posed any problem when it comes to the application of sector-specific regulation. Thus, even though these companies do not fulfil the requirements for the application of specific legislation on consumer credit, it is unknown whether this issue has been so far challenged before Spanish courts.

VI. National legal framework applicable for over-indebtedness

1. What are the possibilities for consumers in case they are considered "over-indebted"?

Debt can always be restructured or reduced (or cancelled[51]) via private agreement of the parties, reached after negotiation or after a process of conciliation or mediation;

- Consumer *bankruptcy*: debt can in theory be partially discharged by order of the Court in bankruptcy proceedings, as a result of the *agreement* of (the majority of) creditors or, in the absence of the latter, where appropriate and with certain pre-requisites, *imposed* by the Judge, after the *liquidation* of debtor assets. However Spanish bankruptcy regulations are profoundly inadequate for consumers and have traditionally entailed disadvantages for their protection, and still incomprehensibly do. For instance, mortgage debt (which constitutes the bulk of household debt) is excluded from the scope of bankruptcy proceedings (and also from the automatic stay of the eviction) as well as a possible debt discharge after the liquidation of the assets, which was absolutely excluded for individual debtors in 2013. This regime, unfriendly to debtors, (marginally more friendly to consumers) leads to a lack of incentive, acceptance, use, and effectiveness of the procedure and the lack of a consumer bankruptcy culture.
- *Readjustment:* was established in the recent regulatory rules and legislation (RD 6/2012, RD 27/2012 and Law 1/2013), though can only be exercised in extreme cases or on a voluntary basis (Code of Good Practices, whose application hinges on the financial institution's adhesion to it).

a. Is there the possibility for the consumer to reorganise debt or obtain debt relief?

- Debt re-organisation and relief are possible, but they commonly depend on the other party's (usually a bank) agreement. They cannot be imposed on the creditor without his consent, with the *exception* of the isolated extreme cases established in the Law.
- A voluntary system of mortgage debt renegotiation has been introduced by the Royal Decree-Law 6/2012, of 9 March concerning urgent measures for the protection of individuals with a mortgage without resources. Seeking to address the social problem of evictions (see below) this *soft law* regulation introduces a "Code of Good Practice" that applies only to those financial institutions who voluntarily adhere to it, and only to those named "particularly vulnerable" individuals with

51 Debt relief or cancellation ("condonación"), which applies on a voluntary basis, should be distinguished from discharge, exoneration or liberation ("exoneración" o "liberación"), that is the one that can arise from a bankruptcy process, where the Judge can order the discharge of all or part of the debts.

mortgages due to their suffering extraordinary difficulty to meet their mortgage obligations.[52] Those with mortgages who are in such a situation may request from the lending bank:

- First, the *restructuring of the mortgage debt* (by "novation" or modification of the contract) that makes its performance viable by the debtor in the medium and long term. It is necessary that the restructuring plan includes a four-year grace period on the repayment of the capital, an extension of the loan repayment term of up to 40 years, and a reduction in the rate of interest applicable, which, during the grace period, will be determined according to the EURIBOR index plus 0.25%.
- After applying these conditions, if restructuring is not feasible, the debtor may ask the lending institution a for a *debt write-down* (remission or reduction*)* over the capital to be repaid, which, at the discretion of the institution, can be 25% of the outstanding principal amount, or the amount paid in interest to that point, or a part of the value of the awarding of the house.
- Finally, if neither of the two previous measures is able to reduce mortgage stress of the debtor to attainable limits for his financial viability, he may seek the creditor bank the "*datio in solutum*," whereby the debtor demands that the bank accept the transfer of the mortgaged property in payment of the outstanding debt, which will then completely and definitely extinguish the obligation (Article 3 of Code of Good Practices).

- A form of debt relief regime has been introduced by Law 1/2013. This Law reforms the regulation of the ordinary monetary enforcement procedure, which in Spain may follow mortgage foreclosure proceedings (in the event that this mortgage foreclosure – the result of the auction - was insufficient to cover the secured debt). The Spanish Civil Procedure Act lays down in Article 579 that "if the proceeds from auctioned or pledged mortgaged assets are insufficient to cover the debt, the enforcement creditor may seek the enforcement of the remaining amount against whomever it may be appropriate". However Law 1/2013 adds a new paragraph 2 to this article, foreseeing the possibility for individual debtors to obtain debt relief, in the terms set out below.

i) How are the terms re-organization and debt relief defined?

The terms are not as such precisely defined, but applied firstly, as explained before, as a result of the principle of contractual freedom. Debt re-organisation and debt relief have been specifically regulated – as readjustment of debts - by Royal Decree Law 6/2012, Royal Decree Law 27/2012 and Law 1/2013, under the framework of foreclosure proceedings (see § 2 of this § VI).

Moreover, a new mechanism of debt negotiation and re-organisation or relief (prior to the declaration of insolvency) has been set up by Law 14/2013 of 27 September on support for entrepreneurs which introduces a new procedure for out-of-court settlement in new Title IX "Acuerdo extrajudicial de pagos", new Articles 231-242. However this mechanism is designed only for individual entrepreneurs, freelancers and small and medium-sized enterprises (not for consumers).

ii) What are the requirements for re-organisation and relief?

Voluntary debt re-organisation or relief require a specific agreement between the debtor and creditor which must be concluded through negotiation, conciliation or mediation.

With regards to the common *enforcement proceeding* coming after the mortgage foreclosure and award of the house (when the approved auction is insufficient to achieve the complete satisfaction of the right of the creditor), debtors can attain *debt relief*, *compulsory* for creditors, since the new

52 See § I.2. of this Case Study, about „vulnerability". Remember this RD considers being such a "vulnerable situation" when all the following criteria are met: all members of the family are unemployed; the mortgage payment is higher than 60% of the net family income; no other family unit property rights to satisfy the debt; mortgage on the only house owned by the debtor and granted for its acquisition.

regulations settled by the Law 1/2013 amending Article 579(2) CPA[53], within five years from the date of the decree approving the house awarding, (if the debtor satisfies 65% of the total outstanding debt, or within ten years, if he satisfies 80%).

iii) How many consumers have had debt reorganised?

Specific figures regarding how many consumers have had debt reorganised cannot be provided given that there are no official records or accurate data available related to that.

iv) How many consumers have obtained debt relief?

The Association of Registrars of Spain issued in 2012a statistics report called "Registration Panorama of Housing Mortgage Defaults" which states that, from the total of 65,778 foreclosure proceedings initiated in 2012 (of which 74.69% were referred to the main dwelling), the *datio in solutum* occurred in 14,229 cases (representing 21.63% of total).[54]

b. What are the requirements for initiating bankruptcy proceedings for consumers?

The same requirements for debtors apply to initiating bankruptcy proceedings for consumers. There is no special consumer bankruptcy treatment, proceeding or regulation related to this. The *subjective premise* for filing bankruptcy is found in Article 1.1 of the Spanish Bankruptcy Act (LC) which states that "the declaration of bankruptcy shall apply with regard to *any debtor*, whether a natural or legal person". The *objective premise* of this procedure is constituted by the state of insolvency (Article 1(2) LC: "the declaration of bankruptcy shall apply in the event of insolvency of a debtor") and encompasses those situations in which the debtor cannot regularly meet her obligations.

Either the debtor or any of the creditors are entitled to initiate the procedure. In the event that the application is submitted by the debtor, they are to justify their debt and situation of insolvency, which may be actual or imminent (i.e. where the debtor is expected to be unable to meet its obligations regularly and timely). This assessment shall be based on any of the following events:

- General default on the current payment of the debtor's obligations.
- The existence of liens corresponding to pending executions affecting in a general way debtor's assets.
- Uprising or hasty or ruinous transfer or concealment of assets by the debtor.
- Widespread violation of obligations of any of the following categories: payment of tax obligations payable during the three months prior to the bankruptcy petition, the payment of Social Security

53 Without prejudice to the provisions of the preceding paragraph, in the event of award of the mortgaged residence, if the auction approved is insufficient to achieve the complete satisfaction of the right of the enforcement creditor, the enforcement proceeding, which shall not be suspended, for the remaining amount shall comply with the following special rules:

a) The debtor shall be released if the liability is covered, within five years from the date of the decree approving the awarding, by 65 per cent of the total amount then outstanding, increased only in the legal interest until the time of payment. It will be released in the same terms if, unable to meet the 65% within five years, they have satisfied 80% within ten years. If the above circumstances were not met, the creditor may claim all of what is owed under the contract provisions and regulations that may apply.

b) In the event that it had been approved a bid or award on behalf of the enforcement creditor or of one who he would have transferred to his right, and they, or any company of its group, within ten years from the approval, proceed to the sale of the house, the remaining debt at the time of the sale will be reduced by 50% of the capital gain on such sale, which will be calculated deducting all costs properly proved by the creditor.

If in the aforementioned time, there is a monetary enforcement that exceeds the amount by which the debtor may be released as provided above, he will be given the remainder".

54 Colegio de Registradores de la Propiedad, Bienes Muebles y Mercantiles de España, Panorama registral. Impagos hipotecarios de vivienda 2012, Centro de Procesos Estadísticos y Servicio de Sistemas de Información del Colegio de Registradores, Madrid, 2012.

contributions and other joint collection during the same period; the payment of salaries and allowances and other derived relations work relating to the last three monthly salaries.

The debtor must apply for the declaration of bankruptcy within two months of becoming aware of the situation of insolvency.

c. Is there a possibility for consumers to attain discharge of debt (Restschuldbefreiung) within bankruptcy proceedings?

Some experts and social organisations have stressed and claimed for a long time that Spain should establish a regulation to allow for the possibility for an individual debtor to be discharged from their debts that they have not accrued through fraud when they find themselves in a situation of actual incapacity to pay due obligations.[55] However Spanish legislators remain reluctant to set up an adjustment of debts and discharge regime for consumers. As mentioned above, Spanish Insolvency law dating from 2003 did not contain consumer discharge provisions under the framework of bankruptcy proceedings, even though all the recent reforms of insolvency laws in other countries have implemented them.

Only a short time ago, a "fresh start" and discharge regulation made its first (and limited) appearance in Spanish law. The aforementioned Law 14/2013 of 27 September, commonly known as the "Entrepreneur's Act" ("Ley de Emprendedores"), with the goal of improving Spain's economic situation and aiming to promote entrepreneurial[56] culture, activity and development, amongst many other measures, introduces certain changes to the Spanish Bankruptcy Act (Law 22/2003: LC). It is within that framework where the law, at last, foresees a kind of "fresh start" regime, by which an individual debtor is able to cancel debts that cannot be satisfied with his present property and assets, through this bankruptcy process. However, the scope of this "fresh start" is quite restrictive and does not solve the problem of inadequacy of the Spanish legislation regarding consumers: it does not apply to public law claims and requires the debtor to satisfy in full certain classes of claims (preferred claims especially, which include those secured by a mortgage or pledge, which is the main or only household debt).

Regardless, it may be said in general terms that Spanish bankruptcy proceedings are aimed at either achieving an "agreement" ("convenio") between the debtor and creditors or the liquidation of the debtor assets. The first solution, the composition agreement (regulated in Articles 99 to 141 LC) includes a detailed repayment schedule as well as limited deferral proposals, i.e. debt moratoria ("esperas"), debt reductions or relief ("quitas") or a combination of both. Furthermore it may include a "viability plan" if the repayment plan is based on the debtor's future cash-flow. This "convenio" is in fact a kind of readjustment of debts and it is supposed to be the preferred solution, although it is not so often in practice.

Court-ordered liquidation (Articles 142 to 162 LC) will occur if an agreement is not reached: if neither the debtor nor the creditors propose such a composition agreement or if no proposal is approved by the debtor, by the required majority at the meeting of creditors or by the court. It is within the framework of that liquidation where the Law 14/2003 foresees the new discharge schemes.

i) How is discharge defined in the national context? (Is there a definition?)

55 Gutiérrez de Cabiedes, P., El sobreendeudamiento...,2009, pp. 201-226; Gutiérrez de Cabiedes, P.,«La liberación de la deuda restante tras la liquidación en el sobreendeudamiento de los particulares»,Il sovraindebitamento civile e del consumatore. Sistemi giuridici europei alla prova del dialogo (coord. Gutiérrez de Cabiedes/Sarcina/Uricchio), Dialogi europaei, Bari, 2014, pp. 289-314.

56 The Law states is intended to support the entrepreneur and entrepreneurship, and an environment conducive to economic activity. It has been –only- in this setting, when the Spanish Law has thought about discharge. A question should arise: if only in this –necessary, of course- environment of entrepreneurial promotion can be provided a due debt discharge. In any case, this scheme may be indirectly applicable to consumers.

The aforementioned regulation embracing a compulsory discharge regime is set up in Article 21.5 of Law 14/2003, modifying the current Article 178(2) of Bankruptcy Law, which is now given the wording:

"The court decision declaring the conclusion of the bankruptcy proceeding of an individual debtor after liquidation of all his assets shall declare the *remission of debts unsatisfied*, provided that the insolvency had not been declared fraudulent nor convicted for offense under section 260 of the Penal Code or for any other offense relating to bankruptcy, and have been satisfied in full the claims against the estate, and bankruptcy privileged credits and at least 25 percent of the amount of ordinary insolvency claims. If the debtor has unsuccessfully attempted settlement of payments, may obtain remission of the remaining credits if the claims against the estate and all privileged insolvency claims were satisfied".

Consequently, this Article talks about "remission of debts unsatisfied" (after the liquidation phase of the proceedings) not providing a legal definition but establishing the requirements for its attainment.

The ordinary readjustment of debts or partial discharge outlined above, the "quitas" (debt reduction) and "esperas" (*moratoria*) are not defined by the Law either.

ii) If discharge is possible, after how many months/years is it possible?

No temporal requirements are set out by the rule introduced in the Bankruptcy Act (Art. 178.2 LC) by Law 14/2003 on support for entrepreneurs (the way the German and Portuguese legislations do through a "period of good conduct" on which the final granting of the discharge depends). Only objective requirements are provided relating to the full satisfaction of certain types or amounts of bankruptcy claims.

iii) If discharge is possible, what are the requirements for discharge?

According to the aforementioned Article 178(2) of the Bankruptcy Law, the requirements for the court decision declaring the remission of unsatisfied debts are:

- the conclusion of the bankruptcy proceedings of the individual debtor after *liquidation* of all his assets,
- the insolvency not being declared fraudulent nor convicted under section 260 of the Penal Code or for any other criminal offence relating to bankruptcy,
- the satisfaction in full of the claims against the estate, secured credits and at least 25% of the amount of ordinary insolvency claims. And, if the debtor has unsuccessfully attempted settlement of payments, just the satisfaction of the claims against the estate and secured credits.

iv) How many consumers have obtained debt discharge?

Since the legal reforms brining about discharge are very recent, there is no data yet on debt discharge under the framework of consumer bankruptcy proceedings[57].

Bankruptcy proceedings are very limited in the case of consumers. The main reason is the inadequate regulation of consumer bankruptcy in attending to the specific needs of consumers and even its discriminatory and detrimental treatment with regard to that given to professionals, entrepreneurs and companies in bankruptcy legislation.

It also happens that consumers and households in Spain usually hold a mortgage loan as a single credit or as the main one; and this credit holds a position of a privileged credit in the legal system including a right to its enforcement and its separate treatment outside bankruptcy proceedings (through foreclosure and eviction). This feature of mortgage loans with regard to bankruptcy proceedings implies that the

57 About the figures on debt relief on the basis of other means (*datio in solutum* in foreclosure proceedings) see paragraph a) iv) of this Section §VI, 1.

eviction cannot be suspended as a result of the request of bankruptcy proceedings. This suspension can only be made if the property is allocated to the business or professional activity, resulting in the lack of incentive and even meaning for consumers or households to resort to this procedure. This might explain why there is no available data on the occurrence and rate of successful discharge.

The Spanish Statistical Office publishes official statistics on other items and figures from which the limited existence of total or partial discharge of debts within bankruptcy proceedings can be verified. For instance, out of the total amount of bankruptcy proceedings which took place in 2012 (8,726), only 927 corresponded to consumer bankruptcy (natural persons without professional or entrepreneurial activity). And from the total amount of bankruptcy proceedings (regardless whether they were consumers bankruptcies or not) only 118 had a proposal of agreement (that can in general include partial debt discharge, moratoria or both). In 2013, out of the total number of bankruptcy proceedings (9,660), only 726 related to consumer bankruptcy;[58] and only 108 had a proposal of agreement. As a result, it can be said that the extrapolation of these figures to consumer bankruptcy proceedings provides evidence that consumer debt discharge has been so far almost non-existent.

d. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

The inadequacy of bankruptcy regulation in Spain (in which consumers could not in any way have their debt discharged, even after the liquidation of their assets) explains the very limited application of consumer bankruptcy proceedings and, subsequently, the absence of any data in this regard.

New provisions on debt discharge (the aforementioned Article 178(2) of Bankruptcy Law) established by Law 14/2013 do not provide any legal time limit for discharge of debt, but simply provide requirements regarding a minimum amount of debt that must be satisfied.. Requirements of minimum amount of debt satisfied are so high that it can be reasonably assumed that it will continue to be very difficult to meet them in order to have debt discharged.

e. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can take recourse to? Please list and elaborate on requirements, legal consequences, and numbers of consumers who have gone through the measures in question.

There are no further mechanisms.

2. Is there a national legal or policy framework for avoiding evictions?

Before the crisis, legal policy in Spain was focused not on avoiding evictions, but on making them more efficient (for the benefit of both the creditor and the debtor). However the financial and economic crisis that Spain is facing has had a large impact on Spanish society. Thousands of Spanish homeowners with mortgages have faced serious difficulties in complying with their obligations or losing their home while financial institutions are recovering mortgaged properties through enforcement actions. This has resulted in large-scale property recoveries entailing considerable and widespread social and economic costs. As a result, the Spanish government decided to adopt certain extraordinary and urgent measures aimed at reinforcing the protection of the most vulnerable individuals with mortgages from eviction, with the purpose of reducing property recoveries that affect the most vulnerable mortgage debtors.

To address this situation, the government first approved the Royal Decree-Law 8/2011 of 1 July concerning measures in support of individuals with mortgages, which is based on two provisions, reforming the Civil Procedure Act (CPA):

- Awarding price: intended to ensure that, in foreclosure proceedings, the debtor receives an adequate price for the immovable property that allows him to minimise the remaining debt.

58 Spanish Statistical Office, Bankruptcy Proceedings Statistics, 2014.

According to the new drafting of Article 671 CPA, the creditor may seek the awarding of the assets (if there is not a higher bid at the auction) for an amount equivalent to or greater than 60% of their appraisal value (this minimum was 50% before, and has been modified in 2013, setting it in 70% if the property is the primary residence of the debtor, and 50% if not).

- Personal property exempt from seizure: the legal limit of that which is "exempt from seizure" is raised. The general minimum value of what cannot be seized from any debtor (always related to the minimum wage) is set up in Article 607 CPA. However, in the event that (in accordance with Article 129 of the Mortgage Law) the price obtained for the sale of the primary residence at a mortgage proceeding is insufficient to cover the secured loan, at the subsequent ordinary enforcement proceeding based on the same debt, the amount that cannot be seized established in Article 607(1) CPA will be increased by 50%, and an additional 30% of the minimum wage for each household member who does not receive regular income of their own.

This reform, that only "touched up some procedural aspects", must be considered a partial and insufficient measure.[59]

The Royal Decree-Law 6/2012, of 9 March concerning urgent measures for the protection of individuals with mortgages without resources, seeks to address the social problem (and related protests) of evictions of people who have lost their home in foreclosure proceedings. Additionally, in order to provide for a voluntary system of mortgage debt renegotiation, restructuring and write-down, including a possible "*datio in solutum*" (soft law explained above), the decree sets out as an additional and interesting protective measure, that the "particularly vulnerable" debtors who fall within the scope of this regulation[60]are allowed to stay in their home (if they request to do so) as a tenant for a period of two years, paying annual rent equivalent to 3% of the total debt outstanding at the time of the delivery of property to the creditor.

When the situation of households was seriously aggravated, the Government passed Royal Decree Law 27/2012, of 15 November, on urgent measures to reinforce the protection of individuals with mortgages. The purpose of this regulation is to reduce the number of evictions. Consequently, its "fundamental aim" consists of "the immediate *suspension*, during two years, of evictions on the families which are in a situation of *special risk of exclusion*". It will apply to judicial and extrajudicial foreclosure proceedings in which the primary home was awarded and to persons who are in a "situation of special vulnerability".

Finally, Law 1/2013 of May 14 on measures to reinforce protection of individuals with mortgages, debt restructuring and social rent ("Law 1/2013") tries to complete and strengthen the rules providing protection to mortgagors. This Law develops four types of measures:

- A moratorium on evictions of debtors at special risk of social exclusion (already established by RD 27/2012, and practically in identical terms to it).
- Reforms in the mortgage market, through amendments to Mortgage Law. The main issues concerned are:

59 Gutiérrez de Cabiedes, P. «El Real Decreto 27/2012, de 15 de noviembre, de medidas urgentes para reforzar la protección a los deudores hipotecarios", Revista de Derecho Concursal y Paraconcursal, vol. 18, 2013, pp. 479-483 ["The Royal Decree 27/2012, of November 15, on urgent measures to reinforce the protection of mortgage debtors", Journal of Bankruptcy and Para-Bankruptcy Law, 18, 2013, 479], in which is done a compendium of all previous regulation. See also Marco Molina, J., „Spanish Law in 2010-2012: The Influence of European Union Law and the Impact of the Economic Crisis", Journal of Civil Law Studies, vol. 6, 2013, pp. 426-434.

60 As explained above, these debtors are those experiencing extraordinary difficulty to meet the payment of their mortgage obligations. This RD considers that an individual is in such a "vulnerable situation" when all the following criteria are met: all members of the family are unemployed; the mortgage payment is higher than 60% of the net family income; no other family unit property rights to satisfy the debt; mortgage on the only house owned by the debtor and granted for its acquisition. See § I.2. of this Case Study, about "vulnerability".

- Limitation of late-payment interest: on mortgages on principal residences to three times the statutory interest rate.
- Out-of-court foreclosure proceeding: the rules on mortgage foreclosure before a Notary, set out in article 129 of the Mortgage Law, have been amended:

- The value set by the parties as the starting price of the property at auction cannot differ from the value, if any, set for the direct judicial foreclosure proceeding, and cannot, under any circumstances, be lower than 75% of the value set in the appraisal used to grant the mortgage.
- The notary is expressly authorised to warn the parties that some of the clauses of the mortgage on which the out-of-court sale is based or which have determined the amount payable may potentially be unfair terms (as a result of *Aziz* ruling).
- Further, what is more relevant: the Notary will place a moratorium on the out-of-court sale if any of the parties can prove that that those contractual clauses could be unfair (grounds for opposition, set out in the new point 4, added to Article 695.1CPA).

Amendments to the judicial foreclosure proceeding in the Civil Procedure Act.

- Control of unfair terms. The Judge, at his own motion or at the request of the interested party, is able to assess the existence of unfair clauses (and warn the parties, granting them a five day hearing: Article 552(1) amended CPA). If clauses are found to be unfair, the foreclosure is either unjustified, or will be carried out but without applying those unfair clauses (Article 561(1) amended CPA).
- New grounds for opposition to the enforcement proceeding have been established (in Article 557(1) CPA, which now deals with the case in which "the instrument contains unfair clauses"). With regards to mortgage foreclosures, the fact that the contractual clauses on which the foreclosure is based or which have determined the amount payable contain unfair terms is established as a new ground for opposition in Article 695 CPA.
- If that ground is upheld, the foreclosure will either be dismissed (if it was based on the contractual clause in question) or it will proceed, without application of the unfair clause (following the *Aziz* Judgement of the CJEU).

Other reforms affect the costs in a principal residence foreclosure (which cannot exceed 5% of the sum claimed), amendments to RD 6/2012, whose scope of application is extended (to apply mortgage guarantors, and in some aspects of the Code of Good Practices).

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (i.e. debt relief)?

- Filing for bankruptcy does not suspend the eviction of the consumer from their house during the proceeding. This suspension can only be obtained during bankruptcy if the property is assigned to the debtor's business; what results is the lack of incentive and even meaning for consumers to resort to this procedure.
- In the framework of enforcement procedures, RD 6/2012 foresees the possible stay of debtors within its scope as a tenant for a period of two years, paying an annual rent equivalent to 3% of the total outstanding debt in the moment of the house awarding to the creditor. And RD 27/2012 and Law 1/2013 establish the aforementioned moratorium on evictions (see previous and next question), whereby persons affected can stay in their homes.

b. Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

Yes. This is the main scope of the Royal Decree Law 27/2012 in the framework of foreclosure proceedings of most vulnerable households (social groups: see requirements discussed above). Those householders whose properties have been awarded to the creditor (most of the times, a bank) can nevertheless stay in their homes for the two years term of that moratorium (in fact, it is only the final

enforcement phase of this process what is temporarily delayed, but not the repossession as a transfer of property).

However, according to the law, it is not possible for householders that have been already evicted before the entry into force of this moratorium to come back and be reinstalled in their homes. This is why the Royal Decree provides the creation of a new social housing fund for renting (with subsidises economic rents) for all those homeless already evicted or facing eviction.

VII. The regulation of credit bureaus

1. How many credit bureaus are there in the country?

There are a number of different credit bureaus in Spain.

One public register is CIR (Centro de Información sobre el riesgo: Information Center on risk), created by Decree-Law 18/1962. It is a public service under the Bank of Spain (Banco de España, BE, hence also known as CIRBE). Other private credit bureaus are:

ASNEF/Equifax: held by the ASNEF (Asociación Nacional de Entidades de Financiación: National Association of Financial Entities), also known by this acronym. It is a database maintained by the consumer credit reporting agency Equifax[61] which draws on the information provided by their partners.

RAI (Registro de Aceptaciones Impagadas: "Unpaid Obligations Registry") property of the "Centro de Cooperación Interbancaria-CCI" (Center for Inter-bank Cooperation[62]) is a record of delinquent debts that describes itself as "file of non-fulfilment of financial obligations". This is clearly one of the largest sources of information on delinquency and defaults in Spain.

EXPERIAN Credit Bureau and its database BADEXCUG: this is a registry of delinquent debts managed by Experian Credit Bureau ("Experian Bureau de Crédito"). This file has information about non-payment in relation to individuals whose data have been incorporated by the member institutions of Experian Credit Bureau.

FIJ ("Fichero de Incidencias Judiciales y Reclamaciones de Organismos Públicos"): Judicial Incidents and Claims from Authorities File, is a database held by Equifax that contains information on debts claimed by legal proceedings and by public agencies to both individuals and corporations, such as bankruptcies, suspension of payments, foreclosures, and other execution proceedings.

There are also other companies specialized in providing commercial credit reports of companies, non-commercial companies or self-employed: AXESOR, INFORMA Información Económica S.A., INCRESA and DUN & BRADSTREET Spain.

2. Are the credit bureaus public or private?

There are both public and private credit bureaus in Spain (see previous question).

If there are both public and private credit bureaus:

a. How many credit bureaus are public and how many are private?

61 The U.S. multinational Equifax Inc. landed in Spain in 1994 via ASNEF, and articulated through the file manager-Equifax ASNEF on Adequacy and Credit Services S.L. (EQUIFAX IBERIAN GROUP S. L.).

62 The „Centro de CooperaciónInterbancaria - CCI" (Center for Inter-bank Cooperation) is a professional non-profit organization, governed by its own statutes, in addition to complying with applicable associations and business legislation.

CCI was created on July 1985, as a result of the joint action of major banking entities and organizations (Banks, Savings and Loans Depositories, Credit Unions), who understood that the resolution of certain common problems would happen through the implementation of cooperative solutions such as the creation of this specific instrument.

There is one public credit bureau (CIR). All other credit bureaus are private.

b. Do the public and private credit bureaus have different functions and / or procedures? Are they concerned with the same data?

Yes. The public CIR is a positive file (recording all financial obligations) but only applies to large sums of money (more than 6,000 euros). On the other hand, RAI, ASNEF, EXPERIAN and FIJ are negative files (which record only defaults).

3. How are credit bureaus compensated?

Credit bureaus and the files they hold are compensated primarily through fees paid by users requesting information, as well as, where appropriate, by member entities; and, ultimately are funded by the budgets of the institutions owning them.

4. How do the credit bureaus collect data?

The CIRBE entities required to report data each month[63] to the CIRBE are: credit institutions (banks, savings banks, credit unions and branches in Spain of foreign credit institutions, financial credit institutions and the ICO –Official Credit Institute), the Bank of Spain, the Deposit Guarantee Fund for Credit Institutions; the Mutual Guarantee Societies; Counter guarantee Societies; and the State Agricultural Guarantee Company.

Data of the rest of credit bureaus (privately-owned files) is provided by "the creditor or person acting on his behalf or interest",[64] who are in practice the member entities of each association or credit bureau.

Asnef-Equifax collects data from the information provided by their partners: basically integrated by financial institutions (banks, savings banks and other credit financial institutions, etc.), telecommunications companies, energy service operators (electricity, water, gas) publishing and insurance companies.

The information in RAI is provided by the banks, savings and loans banks and credit unions.

EXPERIAN-BADEXCUG collect data from its member institutions, mainly from banking, telecom and insurance companies; but also from companies providing basic services, like water, gas or electricity.

The FIJ file draws on the information provided by publicly available sources (Official Gazettes, Courts and media).

5. In what way do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

The legal framework of data protection is provided by the Organic Law 15/1999 of 13 December, on the protection of personal data ("Ley Orgánica de Protección de Datos"-LOPD) which transposed the Data Protection Directive 95/46 into Spanish law. In 2007 the Spanish Government implemented Organic Law 15/1999 by way of the Royal Decree 1720/2007 of 21 December approving the Regulations implementing the Act. Credit bureaus have to comply with various laws and regulations,

63 Data reported to the CIR by entities shall be accurate and updated, so that they reflect faithfully the situation of the risks and their owners.

64 Pursuant to Article 29.2 of Organic Law 15/1999 and Article 37.3 of Royal Decree 1720/2007, cited in the text, that allow personal data relating to the fulfilment or non-fulfilment of pecuniary obligations to be processed.

ranging from national laws on the protection of personal data,[65] to the ones referred to consumer protection and banking laws, as to specific credit reporting acts.

Spanish legislation sets very strict criteria in law, safeguarding individual freedoms and sanctioning irregularities. These bad debt records are those legally defined in Article 29 LOPD as "information services on creditworthiness and credit". Article 29 of the Data Protection Act (LOPD) regulates the conditions for the lawfulness of the processing of personal data. Further, the rules fixing the LOPD are complemented by articles 37 to 44 of Royal Decree 1720/2007.

The AEPD – the Spanish Data Protection Agency, ensuring the compliance with the legislation on data protection, must guarantee that credit bureaus or delinquency records carry out their work, respecting at all times the requirements for the registration in such "solvency files" (specifically, the prior existence of certain debt, overdue and enforceable, which is unpaid). And, afterwards, must ensure respect for the rights of information, access, rectification, objection to and cancellation of data.

Spanish people are increasingly aware of their rights with regards to data protection legislation and of the role of the Spanish Data Protection Agency.

6. What data is collected by credit bureaus?

- CIRBE. Entities report to the CIR almost all (there are some exceptions) of their credit risks, direct and indirect, including personal data about the holder and the most significant features of risks (debts). In general, the minimum amount of the report is €6,000. CIR manages a database on which appear virtually all loans, credits, guarantees and risks in general. This is a positive, centralised and public register. Its purpose is not only to provide necessary information to reporting entities for their activity and creditworthiness assessment of borrower , but also to allow the Bank of Spain to properly perform its duties and, in particular, the supervision and inspection of banks, especially relevant in the current situation.

Declared risks are classified into two groups:

- Direct risks. These are derived from loans or credits (essentially guarantees) and leasing operations, as well as fixed income securities held by the entity, excluding those issued by the Central Government.
- Indirect risks. These are those who guarantee or endorse other clients who have loans or credits granted by the entity. For example, guarantees, sureties and personal guarantees and firms that have been taken into account by the reporting entity for the assumption of risk.
- The RAI file collects information on defaults by companies, for amounts equal to or greater than 300 €, occurring in documents acknowledging the debt (accepted bills of exchange or promissory notes, and current account cheques or current account promissory notes, not paid when due). The information provided by RAI includes total number of unpaid drafts on record for the company, total value of all unpaid drafts and date of last recorded debt.
- The EXPERIAN/BADEXCUG file has information about non-payment by individuals whose data has been incorporated by any member of this institution.
- The FIJ file includes debts claimed by a number of legal proceedings (such as bankruptcies, suspension of payments, foreclosures, and other execution proceedings), as well as by public agencies (such as National Treasury, Regional Treasuries, Municipalities or any kind of Tax Administration, Social Security, and other types of official debts such as traffic fines).

7. Who are the users of credit bureaus?

65 Personal data is defined as any information concerning identified or identifiable natural persons. "Data with special protection" includes personal data which reveal the ideology, trade union membership, religion, beliefs, racial origin, health or sex life. Each category of personal data is afforded its own level of protection.

Banks and financial entities are the main users of credit bureaus. Records on them are usually required (among the economic risk analysis documents) and inspected closely by banks, before the credit is given, but their information is also required by retail sales, telecommunications, utilities, media, insurance, automotive, leisure, e-commerce, industry, and real estate companies.

The RAI file data can be directly managed only by CCI partners, as long as the consulting entity also provides data on its customers defaults. The CCI organisation web site sets out who its members are (i.e. providers and users of the RAI information). There are 232 CCI partners, consisting of 93 banks, one official credit company, 55 savings and loans banks and 83 credit unions.[66]

This information was originally used exclusively by national banks and credit institutions in order to discover and evaluate the solvency of their clients before approving credit and other bank products. However nowadays interested third parties (mainly, credit reporting companies) have been authorised to access to the RAI. As such, the RAI also provides a payment service, accessible only to users who are in one of the following two cases:

- Creditors: natural or legal persons who can prove they have a loan granted or requested by a legal person; they can only access for granting credit or for monitoring previously granted credits.
- Credit reporting companies: those whose purpose is the activity of providing commercial credit reports; they have access only to serve customers with the purpose of granting credit or monitoring previously granted credits.

Over-indebtedness of consumers

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country? Elaborate.

Yes. It can be said that Spain is the paradigm of a real estate bubble in Europe (that was called "the European miracle") together with the United States and Dubai on the global level. The price of housing increased exponentially, resulting in a huge overvaluation of real estate;[67]the price of a first home in Spain skyrocketed.[68]

When the housing bubble burst in 2008 (a sharp decline in the number of property sales, a drop in housing prices, a steady increase in defaults, etc.) the credit system was significantly affected, having a huge impact on real estate, the cornerstone on which the Spanish economy was hitherto based. The sharp drop in real estate sales in Spain caused an overabundance in housing stock because, until then, the economic policies had strongly promoted the creation of properties as an economic driver of the country.[69] In view of the oversupply, many companies related to the building sector were forced to declare bankruptcy, as well as those economic sectors that revolved around the sale of property.[70] Thus, the housing crisis affected a large number of sectors appendages: real estate, legal, technical (architecture), household services (plumbing, painting, etc.) inter alia; which also had expanded

66 See http://www.asociacioncci.es/cci/en/informacion/componentes/

67 On the issue of overvalued housing in Spain, see The Economist, Global House Price. Ratio Rentals, Dec 30th 2009.

68 Fundación de Estudios Bursátiles y Financieros, El endeudamiento de los hogares españoles, Madrid, 2004.

69 Vid., inter alia, Fernández Durán, R. (2006), El tsunami urbanizador español y mundial sobre sus causas y repercusiones devastadoras, y la necesidad de prepararse para el previsible estallido de la burbuja inmobiliaria, Virus Editorial (Marcial Pons).

70 In 2008, the closure of around half of the real state agencies in Spain was announced. Vid.

http://elpais.com/diario/2008/01/17/economia/1200524403_850215.html. By way of example, in 2008, the Real Estate Network Don Piso, which had become one of the biggest as a result real estate boom, closed most of its offices and fired 350 out of 420 employees after reporting sales dropping by 66% (http://www.elmundo.es/mundodinero/2008/05/25/economia/1211720850.html).

rapidly (the so-called booming effect) as a result of previous conditions of the real estate market during the housing bubble.

2. What is the relation between housing prices and over-indebtedness?

There is a direct link between the increase in house prices and over-indebtedness. Everyone wanted to purchase immovable property, and also to take "part in the game" (i.e. to buy real estate not only for living in, but also – or even simply – to speculate), based on the general conviction that housing prices could never go down. That "game" led to irresponsible lending and borrowing practices, and to an inconceivable rise in household indebtedness that ended in a pathological situation of domestic over-indebtedness, until the housing bubble burst.

According to the UN Committee on Economic, Social and Cultural Rights, the gap between income levels and housing prices in Spain, combined with rising unemployment, have an effect on increasing the rate represented by housing costs on the income. This is translated into an increase in defaults, foreclosures and, ultimately, in the number of homeless people, especially among the poorest and most vulnerable, given their lower resistance to economic shocks and lack of payment capacity.[71]As a matter of fact, the Bank of Spain highlighted that 85% of mortgages that could not be paid in 2012 were taken out in 2007 or earlier, during the housing bubble.[72]

a. How have housing prices developed since 2000 (or later if earlier data not available)?

Data by the Spanish Statistical Office "Mortgage Statistics" and "Housing price index" show how the average amount of granted house mortgages has evolved since 2003 (the first year to have records) to the present.[73] In 2003, with the housing bubble already emerging, an accelerated increase in housing prices was already initiated, lasting until 2008. The average mortgage increased from €93,653 in March 2003 to €116,011 in September 2004 (almost a 25% increase in just a year and a half). In the autumn and winter of 2007 the average mortgage was a maximum of €150,000, an increase of 30% in comparison to 2004. From this period come most of the serious mortgage problems that Spanish households are now facing.

Since the crisis, mortgages have remained in amounts close to 140,000 Euros during a few months. It was after the summer of 2008 that the average mortgage began to drop noticeably. Thus, it went from €134,247 in September 2008 to €119,503 only six months later. Furthermore, mortgages ranged between €115,000 and €120,000 in 2009 and 2010 until in 2011 the crisis intensified and mortgages fell again, both in number and in amount, up to the current minimum, €96,676 in March 2013. Currently, prices have slightly risen to €100,000 (the average value in 2013 was €101,494).[74]

b. How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available?

According to several analyses of the data from the financial survey conducted by the Bank of Spain every three years, the economic crisis and excessive indebtedness have caused serious financial problems at all income levels. In the whole population between 2002 and 2008 the number of households with difficulties in dealing with payments on their debts doubled to 16.5% of the indebted

71 Comité de DerechosEconómicos, Sociales y Culturales, Observaciones finales sobreEspaña (E/C.12/ESP/CO/5), § 21; Amnesty International, Spain: Submission to the UN Committee on Economic, Social and Cultural Rights, 48th session, May 2012, EUR 41/005/2012 (London, 2012).

72 Bank of Spain, Nota informativa sobre la presentación de una nueva estadística de procesos de ejecución hipotecaria sobre viviendas, Available at http://www.bde.es/f/webbde/GAP/Secciones/SalaPrensa/NotasInformativas/Briefing_notes/es/notabe10-05-13.pdf.

73 Mortgages Statistics available at: http://www.ine.es/dynt3/inebase/en/index.htm?padre=1042&dh=1; Housing Price Index at http://www.ine.es/jaxi/menu.do?type=pcaxis&path=/t07/p457&file=inebase&L=1.

74 Spanish Statistical Offfice, Financial and Monetary Statistics, Madrid, 2014.

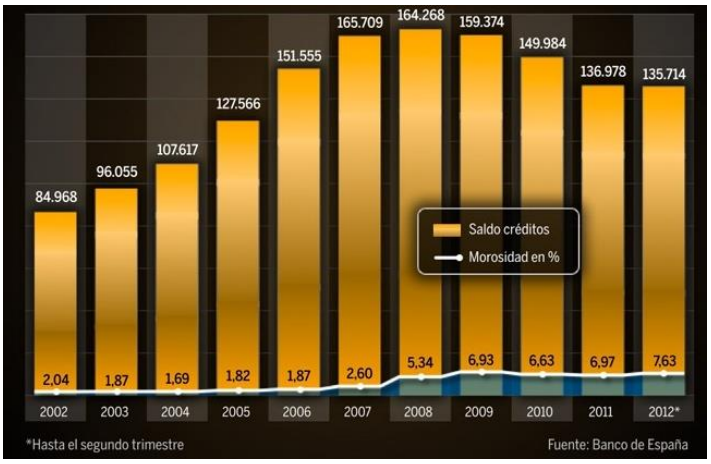
households.[75] As a result of the crisis, the incidence of this problem has grown especially in household with average incomes, ones headed by the young, the elderly, by salaried employees and retirees.[76]

3. *Has there been increased access to mortgage credit? In which way? For example: was access to consumer credit facilitated through legislation? Elaborate. And has access to credit become more restricted since the crisis? Elaborate. If possible provide data.*

Given that the housing market was growing at a high speed during the boom days of real estate, lenders were willing to give credit not only on the value of the property but, in many cases, exceeding that amount. Lenders also encouraged those consumers who did not possess even minimum savings to purchase property to access to the credit market (so-called subprime loans).[77] Thus, the bank concluded "attractive" contracts with consumers who saw in this practice a "favourable" way (apparently at low interest rates) to access to purchase property. A scenario of low interest rates led many people to a high level of indebtedness. In fact, easy access to mortgage credit provided by banks as a result of a flexible policy of lending, facilitated the housing boom. The increase in housing prices is closely linked to the increase in the value of credit contracts.

Nonetheless, since the crisis, access to funding has been an increasingly difficult task for families and SMEs, both in terms of quantity and conditions of available bank credit. Banks are not willing to lend anymore; available credit terms and conditions have tightened. Increased default rates coupled with risk aversion is exacerbating the negative conditions to access to credit (with low expectations that the situation will get better in the short term).

Evolution of consumer credit. Millions of Euros and default as a percentage.



Source: Bank of Spain

Despite policy statements from the Government stating that financial entities should allow consumers access to credit since the money used to bail out such institutions came from taxpayers, and despite the announcement of a boost in the activity of the Official Credit Institute (Instituto de Crédito Oficial, ICO) with new policies to facilitate access to credit, the flow of credit to families and SMEs has not actually been facilitated or favoured.

75 Consejo Económico y Social, Memoria 2012.Calidad de vida y protección social, 2013. [Spanish Economic and Social Council].

76 Valiño Castro, A., Efectos de la crisis en la accesibilidad a la vivienda de las familias en función de su composición y residencia. Información Comercial Española, ICE: Revista de economía Nº 867. Economía de la vivienda en España. Julio-Agosto 2012.

77 For further information on this regard, see the section dealing with Creditworthiness Assessment in this contribution (below).

4. *What is the relation between employment and over-indebtedness?*

   a. *How many percent of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when*

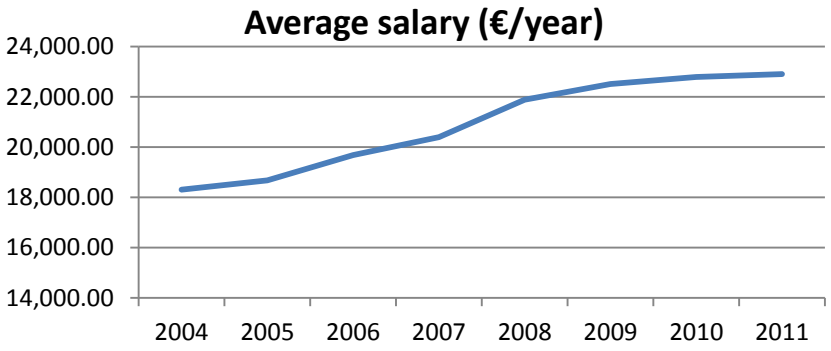
      i) the credit contract was signed

      ii) over-indebtedness arose?

There is also a rather clear relation between (un)employment and over-indebtedness. The end of housing bubble has entailed the decline of the real estate market and the loss of millions of jobs directly and indirectly related to the real estate sector. Although no accurate statistics are available on this issue and the relation between these two variables, it can be said that most of the over-indebted consumers (and families) who afterwards lost their employment were fully or partially employed when the credit contract was signed.

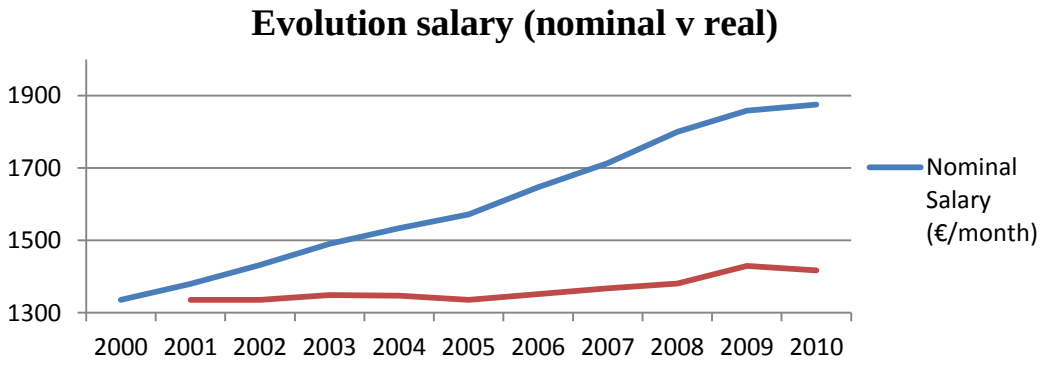
   b. *How has the average salary evolved since 2000?*

The average annual earnings per worker was €22,899.35 in 2011.[78]



Source: Spanish Statistical Office, Wage Structure Survey

It is important to remark here that this evolution corresponds to nominal salaries; i.e. that the evolution of real salaries is not so pronounced. The increase in salaries was compensated (and practically annulled) by the increase in the Retail Price Index (around 85% of salary increase was "swallowed" by the RPI.) Thus, real salaries have actually increased only by €82.11 per year.



Source: Spanish Statistical Office and Spanish Journal (Expansion)

78 Latest data available.Spanish Statistical Office, Wage Structure Survey; available at http://www.ine.es/jaxi/menu.do?type=pcaxis&path=/t22/p133&file=inebase&N=&L=1.

5. *Non-EURO countries: Did national monetary policy play a role in consumer credit and mortgage agreements?*
   a. *Are/were foreign currency loans common?*
   b. *What are the foreign currencies in which loan agreements were concluded?*
   c. *Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?*

----------Not applicable----------

6. *Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?*

Yes, the lack of credit (in many cases that could and should have been reasonably given) and the austerity measures in place are making it harder to solve the financial problems of many consumers and households.

IX. Micro-economic risk factors for over-indebtedness (consumer behaviour)

1. *What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)*

Most consumer credit is devoted to acquisition of immovable property (mainly habitual residences: see above). At the beginning of 2000s, consumer credit (e.g. credit-card lending and loans for general consumption or moveable goods acquisition) started to lose ground as a percentage of the total against residential mortgages (considered more secure because of the attractive and always "profitable" prices of houses). According to the Bank of Spain "Survey of Household Finances", in December 2007 more than 55% of the total debt amount corresponded to payment arising from the acquisition of the main dwelling.[79]

2. *How many credit agreements do consumers conclude on average?*

There is no data on the number of consumer credit concluded on average. An average consumer or householder has at least one credit (mainly, a mortgage) and many of them more than one: typically, car loans and more than one in five have other credits such as a student loan or for purchasing house furniture and even holidays. It is unusual to accumulate more than two loans on the mortgage credit.

Moreover, in general terms, a clear decreasing trend can be observed since the crisis: Spanish consumers conclude far less credit agreements than before. From the lender's side, because banks have drastically restricted granting of credit; and from the borrower side, some because of their over-indebtedness situation, and others, due to caution as a result of the crisis.

3. *Was/is the housing market in the country based on rent or ownership?*

A "culture" of housing ownership for everybody was established in Spain in the 1980s and 1990s; and it reached its zenith in the years of the housing bubble (economic boom, continuously rising prices etc.). At that time, the rate of home ownership in Spain was 83%.[80]

79 Banco de España, "Encuesta financiera de las familias (EFF): Métodos, resultados y cambios entre 2002 y 2005", Boletín Económico, diciembre 2007, pp. 33-65. [Survey of Household Finances]

80 Andrews, D.;Caldera Sánchez,A., «The Evolution of Homeownership Rates in Selected OECD Countries: Demographic and Public Policy Influences», OECD Journal: Economic Studies, 2011, vol. 1, p. 212; European Central Bank (ECB), "Eurosystem's first Household Finance and Consumption Survey (HFCS)", ECB Statistics Paper Series, No 2 / April, 2013, pp. 24-29.

At the start of the financial crisis, and with thousands of families losing their homes, the country has been forced to recover the rental market, both in policy and culture.

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if data available)? Please provide absolute numbers and percentage as of population/home owners/indebted consumers/over-indebted consumers.*

Number of mortgage agreements concluded per year:[81]

2003 1,357,242

2004 1,608,497

2005 1,798,630

2006 1,896,515

2007 1,780,627

2008 1,283,374

2009 1,082,587

2010 960,948

2011 651,759

2012 274,715

2013 325,441

5. *How many indebted and over-indebted consumers have credit card debt?*

There has been a growing trend towards using credit cards since 2000 until 2008[82]. Nearly all over-indebted consumers have credit card debt. Before the crisis, credit card lending was common banking practice. Banks tended to sell a "package of products" in which it was included, at the same time when the mortgage was awarded. Estimated calculations stand at about 6,500,000 consumers who have credit card debt in Spain.[83]

a. *How high is this debt?*

Although the total number of credit cards has dropped from the start of the economic downturn, since then the financing needs of consumers during the crisis have helped to considerably raise the debt. Unofficial estimates from the figures of the ECB and industry consultants suggest that outstanding balances grew from nearly €26.00 billion in 2005 to €70.00 billion at the end of 2010, and to an estimated figure of €89.00 billion at the end of 2012.[84]

b. *How long does it take consumers on average to repay credit card obligations?*

81 Spanish National Statistical Office. Mortgages annually constituted. Rural and urban.Data available at http://www.ine.es/jaxiBD/tabla.do?per=12&type=db&divi=HPT&idtab=19. 26th September 2013.

82 This year, it reaches the maximum of 44.82 billion. The credit cards in Spain began to decline with the recession of 2009. The total number of bank cards (aggregate of debit and credit cards) in Spain also began to decline from 2009, after peaking at 76.4 million. Since 2008, the total number of cards has declined just a tenth, 7.6 million, but less on credit cards (3.4 million).

83 Estimated calculations provided by Adicae, Spanish organization of banking services.

84 http://www.publico.es/dinero/459182/la-crisis-cuadruplica-la-deuda-de-los-espanoles-con-sus-tarjetas-de-credito

There is no public or private data regarding the average period of repayment of credit card debts with the necessary level of accuracy. However it can be certainly stated that the ordinary repayment period offer without additional cost is between one and three months.[85]

6. *What percentage of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?*

The amount of overdrafts increased by around 27% in the last five years until 2012. In April 2012, the amount of overdraft debt reached €38,760 million Euros. That was 7.11% more than the same month last year (and 27% more than that recorded before the economic crisis began five years ago).[86]

   a. *How high is this debt?*

The highest record was published in 2009, when it amounted to €45.10 billion in overdraft facility debt.

   b. *How long does it take consumers to repay overdraft facility obligations?*

No data available. Spanish Statistical Office gathers information of households that face overdraft facilities debt but not concerning its repayment period.

7. *Is there a relation between the length of the credit obligation and over-indebtedness?*

   a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*

Yes, but this is due to the predominance of mortgage credit in the total amount of consumer debt, and its long term debt.

   b. *How long are the time periods for which consumers took on credit and mortgage obligations? Is there a difference in data from before and after the crisis?*

In contrast to "traditional" loans of ten to fifteen years with double-digit rates, from the start of the housing boom banks began selling mortgages for 20, 25, 30 and even 40 years (at very low interest rates), in this way lowering the monthly fee payable to very affordable levels for a vast majority of the population. In 2007, the time frame grew to 35 years in 79% of banks and 47% of them came if necessary to accept up to 40 years.[87] However, the average lifetime (the real repayment term in practice) of residential mortgage loans has been much lower.[88]

   c. *What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?*

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85 Spanish Statistical Office gathers information of credit card debt, but no its repayment period.

86 «Las cuentas en `números rojos´ se desbocan por la crisis»,

http://www.finanzas.com/noticias/economia/20120624/cuentas-numeros-rojos-desbocan-1427775.html#VwZ1dMXraW9WVIqO

87 Adicae, La realidad del crédito en España, Madrid, 2007, p. 18. The average duration of loans and mortgage loans varies something depending on the mortgage loan type of interest:

a) the variable rate mortgages were usually offered with the option of longer maturities: typically between 20 and 30 years (the most common term) or even more (40 years-term loans were offered and contracted); b)fixed rate mortgages usually have a repayment term of 20 years.

88 According to the data producing Spain Mortgage Association (AHE), published in the Economic Journal Cinco Días. (http://cincodias.com/cincodias/2012/11/13/economia/1352946216_850215.html.) in 2002, it was 8.8 years and reached down to just 7.7 in 2003. This is so for two reasons: the first and most common, the so-called "replacement purchases"; and the second, the "capital prepayments". Now, with the explosion of the crisis, wage cuts, increasing unemployment and rising prices and taxes, most mortgage holders have enough with complying promptly with their receipts, what explains that the effective average period has increased from those 8.8 years to 13.2.

We think that the default of the consumer is more linked to personal circumstances and general economic situation than to longer or shorter lending terms. There would not have been much difference (in terms of non-compliance) if, instead of 30-40 years term loans, have been signed 20 years term ones. It has been more a matter of widespread irresponsibility in the credit market or policy (lack of creditworthiness assessment, speculation, etc., but as part of it also the long term).

X. Relation between income and (over-)indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

In 2012, Spanish households spent most of their budget in the following items:[89]

- Housing, water, electricity and fuel; average expenditure per household was €9,090 and accounted for the 32.3% of the total household budget.
- Food and non-alcoholic beverages, amounting to € 4,141; 14.7% of budget.
- Transport, with an average expenditure of €3,321, had a weight of 11.8%.

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

Yes. Even though there is no official data about contracting differences according to income level, it was unfair common practice to subject low income consumers and immigrants (the so called "NINJAs") to more onerous obligations, and to require them to buy other financial products such as house insurances.

   a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate this risk through higher interest rates?)*

As stated above, although there are no explicit different interest rates depending on the higher or lower income of the borrower in Spain, low-income consumers were not given the best market conditions mortgages, due to their consideration. Even today, during the recession, some banks offer mortgage loans in very competitive conditions (interest rate) that, in the sight of their conditions, are targeted to high income consumers.[90]

   b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

See previous questions: if they were subject to less advantageous terms than high-income consumers (higher spreads and therefore interest rates, or higher terms) they would end up paying more.

   c. *Are there other key terms, which change according to the income of the borrower?*

Most important differences (related to the income of the borrower) are the above mentioned factors relating to the requirement for collateral or other disproportionate personal guarantees and other "linked" bank products.

89 Spanish Statistical Office, Household Budget Survey, 2012.

90 See the new http://www.idealista.com/news/archivo/2010/03/09/0151125-bankinter-lanza-atractiva-hipoteca-clientes-rentas-altas ("Bankinter launches mortgage with low commissions for high income customers") were it is explained that Bankinter wants to catch high-income customers and has therefore launched a new variable rate mortgage with a spread of 0.35%, the lowest in the market. The loan is destined to the purchase of homes with appraised value exceeds € 300,000".

Behaviour of actors in relevant cases

This study is empirically and statistically underpinned by:

- a set of meetings and additional written submissions with bank officials of Spanish major Banks (Banco de Santander and BBVA) with relevant expertise and knowledge on lending practices (mortgage and general) and representatives from consumer organisations with specialised knowledge on consumer credit and indebtedness issues (generally, from the Spanish Consumer Association ADICAE[91]);
- and hence, on extensive field research based on interviews of 3,960 consumers representative of different age, sex and place of residence in Spain, conducted by the aforementioned consumer organisation, specifically on issues covered in this case study.

XI. Irresponsible lending practices

1. Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)

The Spanish housing bubble gave rise to a vicious cycle. Advertising was "aggressive", banks were remarkably active in taking the initiative in relation to lending, intermediaries contributed to this phenomenon, and consumers also demanded access to loans. The result was a "circle of greed" that resulted in the financial crisis.

2. Was a creditworthiness assessment undertaken before granting the credit?

a. In how many cases were creditworthiness assessments undertaken?

Creditworthiness assessments were actually not ordinarily undertaken in most cases. In the years of the real estate boom (mainly, 2003-2008), mortgage lenders approved loans for borrowers without carefully examining their actual ability to pay and comply with their obligations and even the bank being aware of data that showed somehow the opposite.

b. Who was the initiator of the creditworthiness assessment?

In the cases it may properly take place, the lender (Bank) was its initiator.

c. Who undertook the creditworthiness assessment?

If any, it was the financial entity (bank or saving bank) who undertook the creditworthiness assessment, as it is explained in subsequent questions.

d. What were the criteria of the creditworthiness assessment?

In the years in which there was some previous control for the allocation of loans, the lender (bank) normally requested the following documents: income tax for previous last years, and the "last pay check" from the time the loan is requested (to prove that the incomes declared in the statement, be the candidate self-employee or employee, are still received). Furthermore, the bank also considers defaults and credit records.

e. Was a credit bureau involved?

Yes. Credit bureaus that were commonly involved in this creditworthiness assessment were the RAI, ASNEF and Equifax, to which the banks made a query of information about recorded defaults.

91 ADICAE consumer association has been selected for this research because it is a leading consumer association in Spain, due to its introduction throughout the national territory and its outstanding activity, as well as being one of the few that are precisely specialized in protecting the rights of financial services' users.

3. *Is there a legal obligation for a mandatory creditworthiness assessment? Is this obligation observed in practice? How are the criteria for creditworthiness assessment in legal provisions?*

Yes. Today there is a legal obligation. Now, Article 14 of the Spanish Act of Consumer Credit Contracts (Ley 16/2011, de 24 de junio, de Contratos de Crédito al Consumo) provides that before the consumer's credit contract is signed, the lender shall evaluate the creditworthiness of the consumer, based on sufficient and appropriate information obtained by the resources employed for this purpose, including information provided by the consumer, at the request of the lender or the intermediary granting credit. The assessment of the consumer's creditworthiness shall be carried out taking into account specific rules on risk management and internal control, applicable according to specific legislation. This legal provision also establishes that if the parties agree to modify the total amount of credit after the conclusion of the credit agreement, the creditor shall update the financial information available on the consumer and assess the creditworthiness before any significant increase in the total amount of credit.

4. *Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?*

In the years prior to the housing a negative outcome implied that the credit was normally denied. However, in the last years of the bubble, it might be said that loans were granted even though banks were aware of the risk having into account the doubtful solvency of the borrower (due to lack of regular incomes or to the existing financial burden). This was the reason why atypical or imbalanced guarantees were requested from third parties, usually borrower's relatives.

Although there is no precise data, it can be affirmed that credit was denied in a very small proportion of cases in the five years before the bubble burst. Explanations for refusal were not usually completely explicit: it was common to say that it had been refused at the "high levels" of the financial entity ("risk control department").

5. *Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?*

It can be said that the average consumer was aware, to a certain degree, of the main consequences of failure; although perhaps most of the consumers did not know the precise scope of some provisions of the loan agreements (as those related to default interest, for example). However, the economic state of affairs did not cause any of the operators to consider (despite the warnings of experts) a possible alteration of the economic situation. Because of this, the lenders did not normally explain to consumers in an explicit way any of the rough consequences of failure and consumers did not demand a more profound explanation on those "more complex" issues.

6. *Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?*

No. It was the general economic and credit situation, together with the expectations of profit of all parties concerned which led to a widespread situation of lack of caution and responsibility. Thus, only the request of atypical and imbalanced guarantees requested of third parties could be regarded as a relative imposition by the lender, in cases of doubtful solvency, that the consumer or borrower had to accept if they wanted to have the credit granted.

According to ADICAE, financial institutions tend to follow a "deliberate process, through seduction, persuasion or pressure, making the consumer to accept financial products or services without being

able to comfortably read written information or even the contract itself and, let alone, to advice or conveniently reflect on them".[92]

XII. Irresponsible borrowing practices– emphasis on mortgage

1. Did the consumer read the agreement before signing?

In many cases the consumers did not completely and carefully read, nor completely understand, all the terms of the credit they were taking. In Spain, this has happened with mortgage loans as with another complex financial product, i.e. the so-called "*preferentes*".

In mortgage agreements, despite the role of the notary in property deals[93] (that includes reading the contract to the parties) formally presiding over the signing of the property sales contract, effort was rarely made in order that consumers actually understood the financial and legal consequences of what they were signing.

In this regard, empirical data shows that most consumers (58% of the population surveyed) who contract a financial product or service usually do not receive information concerning the service or product. As a matter of fact, it is usually the bank officer who performs marketing strategies. In addition, where prior information is provided, 48% of the surveyed consumers have reported that information is not appropriate and it does not allow a proper understanding of the specifics characteristics of the product or service; and only 24% profess to have received proper and sufficient information.[94] Notwithstanding this, only a third of the surveyed consumers declared to carefully read the contract.[95]

2. Did the consumer compare (or have the opportunity to compare) deals before entering into an agreement?

It depends on the consumer initiative. This point has not been a problem, at least, in Spain. Perhaps it could be that in some cases there were not real different offers (in essential terms of the contracts) in some products between different banks. But the competition between them (a kind of battle to attract customers) made different offers possible, as well as to be able to compare them.

3. Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?

Of course, in theory, the consumer has the opportunity to ask for explanation before signing the agreement if he has any kind of doubt. In fact, a number of factors like the formality of the act and some (not so unusual) fraudulent practices in which all the parties took part (as it is often the case, the value appearing on the deeds of the property being sold is less than the overall price of the sale, and the notary generally "turning a blind eye"); made more difficult for the consumer to stop and delay the act asking for such explanations. According to ADICAE, a high number of consumers reported that

92 ADICAE, Los hábitos y experiencias de los consumidores ante la publicidad, la transparencia al contratar y las reclamaciones en consumo financiero, 2014. This statement is based on the results of the mentioned survey (hereinafter, Survey among 3,960 consumers). The sample also reports that the 53% of consumers surveyed did not receive any kind of document containing information concerning the features of the product or service. As for aggressive practices, the report shows that a third of consumers (33%) has been forced at least in one occasion, to purchase a product or service against their will.

93 Mortgage loans are always signed in front of the Notary. The Spain's Notary role is to guarantee the legality of the deal and, among other things, to ensure that property buyers or sellers are aware of what they are signing.

94 Survey among 3,960 consumers, Adicae, 2014.

95 Survey among 3,960 consumers, Adicae, 2014.

information provided was insufficient.[96] Furthermore, 39% of the surveyed consumers claimed that they were not allowed to take any document containing information out of the financial institution's premises. Additionally, those consumers who asked for clarifications (68% of the surveyed consumers) asked for explanation before signing the agreement. However, consumers generally evaluate positively the received information (grade 2.75 out of 5).[97]

4. *How much time did the consumer take before signing the agreement?*

In the case of mortgages loans, it may take around one month from the time when the mortgage is requested until the deeds are signed.

5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

Both Article 28 LCC (Ley 16/2011, de 24 de junio, de Contratos de Crédito al Consumo - Law on Consumer Credit Contracts, transposing Directive 2008/48) and Article 10 LCDSF (Ley 22/2007, de 11 de julio, sobre comercialización a distancia de servicios financieros destinados a los consumidores –, on Distance Marketing of Financial Services) provide that the withdrawal period is fourteen calendar days (similar to that provided for in the Consumer Rights Directive). Both legal provisions establish that, as to the criteria for calculating the period, it shall commence on the date of signing the contract or, if it is later, on the date on which the consumer receives the contractual terms and the information required by the respective laws (Article 16 which contains a broad list of data related to the legal and economic contract terms that the lender shall –compulsorily– provide to the consumer).

Consumers do make use of this right regularly, having started to become an integral part of the legal and financial culture of the Spanish average consumer. However, Spanish legislation does not provide the borrower with a right of withdrawal in mortgage agreements.[98]

Litigation

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*

Yes. The leading case on this matter (apart from the issues raised by the *Aziz* case in relation to foreclosure legislation) is clearly the one related to the so-called "floor clauses" ("cláusulas suelo") that several Spanish banks and savings banks have included in their mortgage loans. Those clauses prevent the interest rate on the loan falling below a certain threshold, even when the benchmark rate used for the calculation (EURIBOR in most cases) drops. As such, these are clauses that do not allow consumers to take advantage of a possible EURIBOR index fall.

   a. *What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?*

National law was applicable. The main emphasis was on contract law, specifically general conditions and unfair terms in consumer contracts.

96 Survey among 3,960 consumers, Adicae, 2014: 69% of surveyed consumers were not provided with written information and, a 14% claim that they did not receive any kind of information (either written or oral).

97 Survey among 3,960 consumers, Adicae, 2014.

98 It does, instead, with a right of early payment; and it is also possible to subrogate the credit. And consumers did make use of this right, especially in the years when competition between financial institutions was encouraged by the legislation.

b. What were the issues in question? (i.e.: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)

The most important issue concerned so-called "floor clauses". On 9 May 2013, the Spanish Supreme Court ("TS") issued a Judgment that found "floor clauses" to be null and void, ordering the defendant entities to remove them from their agreements and to refrain from using them hereinafter in the form and manner in which they had been doing[99]. However, the TS rejected the claim consisting in the declaration of nullity of all floor clauses contained in mortgage loan agreements entered into with variable interest rates signed with consumers. The Supreme Court accepted the arguments put forward by the Consumer Association that these clauses were abusive General Conditions and detrimental to consumers and considered the floor clauses used by these banks to be null and void for the following reasons:

- The floor clauses are General Conditions as banks and savings banks impose them on Consumers. The latter are not offered the option of negotiating or to eliminating such terms and merely have to accept them or not sign the agreement.
- They do not specify that the floor is an essential item of the contract. Thus, they lack sufficient clarity and transparency to enable the consumer to perceive that they are clauses defining the main purpose of the agreement, which affect or may affect the content of his obligation to pay, as well as to have a real and reasonably complete knowledge of how they play (or could play) out in the financial aspects of the agreement.
- They cause a significant imbalance in the rights and obligations under the agreement, to the detriment of the consumer. In reality the risks of the fluctuation of the minimum reference rate in the terms contained in these clauses provide coverage exclusively of the risks that the lender may have of downward fluctuations, frustrating the consumer's expectations of cheaper credit as a result of the reduction of the interest rate agreed as variable. Hence, the Court maintains that although the loans are offered as variable interest loans, the height of the floor in the clauses examined converts them into fixed rate loans, variable only on an upward basis. Hence, the clauses are abusive and detrimental to the consumers.[100]
- Therefore, the offer of variable interest not completed with adequate information is misleading for the consumer, especially in cases where his attention is diverted and analysis of the impact of the floor clause is made more difficult through the joint offer of ceiling clauses.
- Likewise, the statement criticises the entities for (1) the absence of any simulations of various scenarios related to the reasonably foreseeable behaviour of the interest rate at the time of signing up, (2) the lack of prior information on the cost comparison with other products of the entity and, (3) in the case of those used by BBVA, their location amongst an overwhelming amount of data among which the attention of the consumer is diluted.

Further clarification was delivered by the TS on 3 June 2013. The TS clarified that there are no specific grounds for determining the lack of transparency of floor clauses, nor specific formulae, the compliance with which would automatically avoid such consideration. The clauses will only be void if they do not enable the consumer to know the real risk relating to the distribution of changing interest

99 The Sentence was ruled on the appeals against the judgment given by the Seville Provincial (Appellate) Court. The latter ruling revoked the judgment rendered by the Commercial Court no. 2 of Seville and rejected the claim made by the Association of Bank Users against BBVA, CAIXA GALICIA and CAJA MAR, declaring that "floor clauses" of the mortgage loan agreements signed with consumers of the aforementioned entities were not null, deeming that the prerequisites contained in the General Law for the Protection of Consumers for them to be considered abusive were not present. The TS, contrary to the reasoning of the Provincial Court, declared the aforementioned clauses null and void.

100 Floor clauses agreed in the contracts ranged from 2.75 to 3.5% (with EURIBOR closing at 0.59%) and ceiling clauses (maximum interest rate) from 12 to 15%: so, there was a disproportionate difference between the floor and ceilings clauses in place, as the high ceiling levels put in place were unlikely to ever be reached, while the floor interest rate is very close to the market interest rate.

rates. Hence, if the clause does not meet any of the transparent demands required by the ruling, it will be immediately declared void.

Moreover, the order states that the nullity of a floor clause is not remedied by the fact that the consumer has benefited for a time from the reductions in the reference rate, since this circumstance does not make it transparent and does not do away with the imbalance that is contrary to the interests of the consumer.

Given the TS's position, the reaction of the defendant banks has not been long in coming, and they have announced the removal of such clauses from their financial instruments. Meanwhile, other banks that are not directly affected by the decision have announced that they will deal with the matter on a "case by case" basis with clients who feel they are affected, but they have no intention of carrying out a mass annulment.

Another relevant issue is to determine whether the annulment of floor clauses apply retroactively or not. The TS has declared the non-retroactivity of the judgment, so that the invalidity of these clauses does neither affect situations definitely decided by res judicata court judgments nor payments made up to the date of publication of the judgment. This means that interest payments made "in excess" by consumers based on clauses declared void are not to be repaid by the financial institutions because, in the words of the Supreme Court itself, "the retroactivity of the judgment would create a risk of serious harm of importance to public policy in economic matters".

Notwithstanding the above, there have been several judgments of First Instance or Appellate Courts that, dodging the position of the TS on retroactivity, are ordering the banks to refund the amounts received in excess from the date on which the floor clause was implemented.[101]

101 Thus, the Court of First Instance No. 4 of Orense, in a ruling dated 13 May 2013, justified this action by saying that non-retroactive application thereof would violate the principle of effective judicial protection, and it would be contrary to Article 1,303 of the Civil Code, which states that the ineffectiveness of agreements - or any of their clauses, if the agreement subsists - requires destroying the consequences thereof and removing all traces thereof, as if they had never existed, and thus avoiding any effects being derived from there.

In the same vein has pronounced the judgment of 23 May 2013, issued by the Commercial Court No. 2 of Malaga. It argues that, as a consequence of the declared nullity, benefits derived from the invalidity of the clause must be returned, also based on Article 1303 of the Civil Code, and "not applying to this case the conclusions reached in the judgment of the Supreme Court of May 9, 2013". It clarifies that judges have "the inescapable duty to resolve the cases according to established system of sources, which establishes the primacy of the law (Article 1303 CC) on jurisprudence". Therefore, amounts unlawfully received are ordered to be returned with legal interests from the date of receipt.

Similarly, the Court of First Instance No. 1 of Barcelona, issued on 31 May 2013, declares that "to admit legal and economic effects to clauses declared void under mandatory rules, as the consumer law, could generate, indeed, serious problems in legal and financial certainty, at least for one of the parties concerned".

The Commercial Court No 1 of Bilbao judgment, dated 19 June 2013, goes further expressly justifying the non-application of the Supreme Court doctrine, and concludes that, as a general rule, the ineffectiveness of any of the contract clauses, if the contract remains "requires destroying its consequences and cover their tracks as if they had never existed." That way, it is avoid that what is null could produce any effect, as provided in Article 1303 of the Civil Code. The small amount at stake in this process, which involves two individuals, becomes the key to order the return of payments. In this case, that is "the only one that this judge must solve, cannot be said that returning to the plaintiff the amount claimed (11,973 Euros) could generate any risk of serious disturbance with significance to public economic policy". "This seems to be, in the light of other circumstances listed, the main reason leading to the Supreme (and the public prosecutor) to pronounce against applying the general rule of retroactive clause void ground. And not is applicable to this case". This judgment retains a degree of *veiled criticism* regarding the TS ruling.

On 27 June 2013 the Badajoz Provincial Appellate Court, although ruling in favour of a bank –Liberbank- dismissing an appeal filed by a customer, pointed out that the floor clause was not included at the signing of the mortgage loan agreement, but rather it was added later, at the customer's request, when both parties signed a novation of the agreement increasing the principal amount of the loan and modifying, among other conditions, the rate of interest by introducing a variable rate instead of the fixed rate initially agreed. For this reason, the Provincial Appellate Court considers that there was a possibility of effective negotiation, not merely illusory, that there was not a lack of transparency and, therefore, that the floor clause should not be declared null and void.

c. What were the predominant issues (before and after 2008)?

This question has been explained in the preceding paragraphs.

2. Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?

In the class action lawsuit in which the TS issued the (Judgment of 9 May 2013) declaring null and void the floor clauses, the plaintiff was the Spanish Consumer Association of Banking Services AUSBANC. Other Consumer Associations as ADICAE and OCU have also filed actions claiming the annulment of such clauses in mortgage loans and seeking the return of amounts paid and also both in class actions and in individual ones.

3. What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?

Consumer associations report a success rate of between 80 and 90% in the litigation concerning "floor clauses". The same success rate can be said to have the claims of the banks against consumers, typically in foreclosure proceedings.[102]

4. Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?

Yes, as included in the Civil Procedure Act (CPA), passed by Law 1/2000 of 7 January,[103] and other laws transposing into Spanish law EU Directives. The provisions enable collective action to be taken to defend the collective and diffuse rights of consumers and users in specified circumstances. The available remedies are typically injunctions (and previous available injunctive relief) and actions for damages, mainly monetary claims.

The rule on standing is laid down in Article 11 of the Civil Procedure Act. The first rule is that "notwithstanding the individual standing to sue of injured persons, the consumers' and users' organizations legally constituted are entitled to bring an action defending the rights and interests of their members, of the association, or the general interests of consumers and users." Further rules deal with who is entitled to sue, depending on whether the persons injured by the tort are determined or not, as outlined below.

If yes:

(Contd.)

See http://www.eleconomista.es/legislacion/noticias/4880300/06/13/Clausulas-suelo-un-juez-ignora-al-Supremo-y-devuelve-el-dinero.html (with a quite illustrative title: "Floor clauses: two judges ignore the Supreme and return money"), http://www.eleconomista.es/legislacion/noticias/4926437/06/13/Clausulas-suelo-tercer-fallo-a-favor-de-devolver-el-dinero.html , http://www.eleconomista.es/legislacion/noticias/4937027/06/13/Cuarta-sentencia-a-favor-de-devolver-el-dinero-por-clausulas-suelo-abusivas.html, and http://www.sjberwin.com/insights/2013/07/15/el-tribunal-supremo-se-pronuncia-sobre-las-clausulas-suelo.

102 Estimated calculations provided by ADICAE.

103 Class action law in Spain originated from within consumer law, emerging in the Consumer Protection Act, approved by Law 26/1984 of July 19, and developed after an enormous tragic event (the mass tort "Colza oil case" in the 1980s) and then with national implementation of EU legislation. However, legal recognition of substantive consumer rights was not accompanied by regulation of procedural statutes and mechanisms to enforce those rights before the courts, but only by a few sectorial legal rules.

Some academic comments criticized traditional procedural laws and schedules as inappropriate to provide legal protection for these new rights and interests, but thorough analysis and jointed proposals were missing (for a deeper analysis, see Gutiérrez de Cabiedes, P., La tutelajurisdiccional de los interesessupraindividuales: colectivos y difusos [Judicial Protection of supra-individual, collective and diffuse interests], Aranzadi, Pamplona, 1999).

The collective litigation phenomenon finally received statutory recognition in the Civil Procedure Act (CPA), passed by Law 1/2000 of January 7, which established a "class action" regime in Spain that could be considered one of the most advanced in Europe.

a. How are those interests defined?

Article 11 of the CPA defines collective those interests as:

- Collective: "When people affected by a harmful event are determined or easily determinable".
- Diffuse: "When people affected by a harmful event would be an indefinite or hardly determinable plurality of consumers".[104]

b. What are the requirements for such representation?

In the first case, Article 11(2) CPA provides that "When people affected by a harmful event are determined or easily determinable, the standing to sue to protect these collective interests belongs to consumer organizations, to legally constituted entities whose aim is their protection or enforcement, as well as to the groups of affected people."

In the second case, pursuant to Article 11(3) CPA:

"When the persons affected by a harmful event would be an indefinite or hardly determinable plurality of consumers, standing to sue for the protection of these diffuse interests exclusively belongs to the consumer organizations that, under the Law, are considered representative."[105]

5. In practice, is litigation in "public/diffuse interest" more common than individual litigation?

Yes. Although the Civil Procedure Act in Article 11(1) gives standing to individuals affected by unlawful actions in consumer law, consumer organisations are those most commonly demanding the protection of public and diffuse interests.

Not only legal, but also practical reasons lead to this. Actions are brought by consumer organizations, from a legal point of view, based on their special statutory purpose, which is to protect the specific interest of consumers as a whole, or of those of specific goods and services. A practical reason relates to the economic and cultural obstacles to access to justice that an individual faces when going to the court, in opposition to an organisation.

6. Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?

104 The Civil Procedure Act alludes to criteria that differentiate between collective and diffuse interests, based on the determination of "class members." But it does not attend to the substantially different nature of multiparty legal situations: a supraindividual interest, that is, hurt that can be satisfied or amended (e.g., by a declaratory or injunctive action), and individual although plural rights (as those enforced by damage class actions) (see Gutiérrez de Cabiedes, P., 1999, 99-113).

The legal drafting seems to be referring to the secondly mentioned. All subsequent articles on this topic talk about the "consumer and users rights and interests" or "collective and diffuse rights and interests" and do not make any differentiation between these multiparty legal situations (plural and supraindividual).

105 See Gutiérrez de Cabiedes, P., „Spain", Annals of the American Academy of Political and Social Science, vol. 622, 2009, 170-179.

The CPA did not define what "representative" meant and this „corporative model" raised many doubts about its convenience and its constitutional adequacy (Gutiérrez de Cabiedes, P., „La nueva Ley de Enjuiciamiento Civil y los daños con multiples afectados", in Derecho del Consumo: Acceso a la Justicia, Responsabilidad y Garantía, 133-202, Madrid, Spain: Ministerio de Sanidad y Consumo—Consejo General del Poder Judicial, 2001, 163-68 [translat: „The new Civil Procedure Act and damages with multiple affected ", in Consumer Law: Access to Justice, Accountability and Guarantee, 133-202. Madrid, Spain: Ministry of Health and Consumers, General Council of the Judiciary]). But this was clarified, after it was highlighted, by Law 44/2006 of December 29, on the Improvement of the Protection of Consumers and Users (providing, inter alia, for the amendment of General Law 26/1984: Consumer Act). Under this law, only associations represented on the Council of Consumers and Users would be considered "representative." Anyway, I suggest that an individual must be entitled to sue to protect his or her interests under the first section of 11(1), and even under art. 24 of the Constitution.

The Spanish legal framework allows for (general) arbitration and mediation, as well as a special consumer arbitration system, and some specific out-of-court dispute resolution devices before financial authorities. Arbitration and other ADR means are increasingly becoming an effective venue for settling civil and commercial disputes in Spain.

Banks increasingly enter into negotiation and mediation proceedings with their mortgage debtors – on a case-by-case basis – trying to reach agreed solutions. They are no longer interested in being awarded more houses, as they will not get enough value to cover the debt in judicial foreclosure, and will merely incur additional costs with the award of the immovable property. Further, debtors are obviously interested in not losing their home and ultimately still owe the bank the amount not paid, plus interests and court costs.

Some Spanish Regions and several Municipalities in the North of Spain have launched "Mortgage Mediation" Programs and Services aimed to intercede with financial institutions in cases of default, to avoid judicial foreclosure and to ensure the best possible conditions in the debt settlement.[106] These are public and free services. They firstly address the economic situation of the family unit and afterwards propose alternatives to settle the debt, with the intervention of expert professionals (mainly mediator lawyers) between the debtors and financial entities.

7. Do consumers make use of out-of-court settlement procedures?

There is no culture of mediation or arbitration in Spain on these matters. Banks and consumers hardly ever made use of out-of-court settlement procedures in mortgage or other loan agreement disputes. However growing international attention to the institution of mediation led to the recent passing of Law 5/2012 of 6 July on mediation in civil and commercial matters, also in this field and it is starting to break through as an alternative to judicial proceedings.

If yes:

a. Which ones?

The Arbitration Act (Law 60/2003) represents a real breakthrough in developing Spanish arbitration as an efficient alternative to litigation and promoting Spain as an attractive seat for arbitrations. Spanish arbitration institutions and practitioners are fully committed to this active arbitration process, leading initiatives to encourage recourse to arbitration in Spain.[107] A relevant feature of the Arbitration Act is the relaxation of the formal requirements of the arbitration agreement and the procedural issues.

The aim of Mediation as enshrined in Law 5/2012 (incorporating Directive 2008/52/EC) is to regulate a fast and effective process of solving conflicts on civil and commercial matters, reducing the burden of litigation weighing down Spanish Courts (supposed to be cheaper than taking the matter to court: no need for a lawyer and a court representative, neither obligation to pay judicial fees). The final agreement or settlement eventually reached by means of mediation is binding on the parties, and is enforceable, being converted to public deed.

The Consumer Arbitration System is an instrument enabling the effective and rapid resolution of disputes between consumers and companies or professionals concerning consumer products and services. It is regulated by the Legislative Royal Decree 1/2007 of 16 November, approving the Redrafted Text of the General Law for the Defence of Consumers and Users, articles 57 and 58; and by the Royal Decree 231/2008, of 15 February, (specifically) regulating the Consumer Arbitration

106 As does the Community of Navarra, with a Plan destined to citizens of that Community who cannot afford to pay the mortgage on their primary residence "for reasons not directly attributable to the family unit"; and the Municipality of its Main Town, Pamplona, the Basque Country Community or the Municipality of Zaragoza.

107 Soundly based on the UNCITRAL Model Law, the Arbitration Act is aimed at harmonising domestic regulations with international arbitration standards and, thus, fostering the development of arbitration in Spain. See Astarloa, E. and Leandro Vieira, P, „Spain", in The Dispute Resolution Review, Law Business Research Ltd, 5th ed., 2013, 784.

System. A large part of consumer disputes can be solved through this system, nevertheless the cases outside the scope of arbitration are those when:

- there is already a previous judicial resolution,
- the parties have no power or right to dispose of the product or service,
- there is a case of poisoning, injury, death or reasonable suspicion of a crime.

The Consumer Arbitration System offers a streamlined procedure free-of-charge (which reaches up to the cost of the tests when proposed by the Board), that will not last for more than 6 months from the beginning of the arbitration). It is also simple (the arbitration form is available on the internet and can be submitted to the Consumer Arbitration Board or any Consumer Office of Regions or Municipalities), and effective (the awards have the same binding effects as a Court sentence).

For out-of-court settlement of cross-border disputes in the financial services sector is available FIN-NET Network, responsible for handling disputes between consumers and financial services providers (i.e. banks, insurance companies, investment firms and others).Currently FIN-NET has three (of its total 56) members in Spain. The main concerned here, the "Servicio de Reclamaciones del Banco de España" [Complaints Service of the Bank of Spain]covers financial institutions (banks, mortgage banks, credit unions) and these financial products: payments, deposits, credit & loans and mortgages.

The ODR framework for the online dispute resolution for cross-border electronic commerce transactions was established by the Law 34/2002, of 11 July, on services of the information society and electronic commerce ("Ley 34/2002, de 11 de julio, de servicios de la sociedad de la información y de comercio electronico"- LSSI). It promotes the development of codes of conduct, of voluntary adhesion, considering them an instrument of self-regulation especially suitable, within which specific alternative dispute resolution means can be created, arising in the electronic activity and contracting, or developed within the "information society".[108]

Administrative mechanisms to protect financial services customers. In the specific area covered by the already cited Law 22/2007, of 11 July, on distance marketing of financial services to consumers (LCDSF), there must be mentioned mechanisms or specific measures to protect customers of financial services established in Law 44/2002, of 22 November, on Measures to Reform the Financial System ("Ley 44/2002, de 22 de noviembre, de Medidas de Reforma del Sistema Financiero" – LMRSF), Chapter V, arts. 22-31.

- First, the Act (Article 29) requires for all financial institutions to have a Customer Service (or an Ombudsman, which shall be an independent entity or expert) who shall be responsible to address and resolve the types of claims to be determined by their operating rules that customers can submit[109]. The Ombudsman's decisions favourable to the claim have a binding effect for the entity. In addition, the Law 35/2003, of 4 November, on Collective Investment Institutions extended this obligation and treatment to collective investment institution management companies.
- Second, some new specific administrative bodies are established: the Commissioners for the protection of customers of financial services (of banking services, of the Investor, and of the Insured and Pension Plans Stakeholders: Article 22). They are organs attached to the Bank of

108 See Gutiérrez de Cabiedes, P. „Comentario al Artículo 32. Solución extrajudicial de conflictos - Ley 34/2002, de 11 de julio, de servicios de la sociedad de la información y de comercio electrónico", Comentarios a las normas de protección de los consumidores (coord. CámaraLapuente, S.), Colex, Madrid, 2011 [„Commentary to Article 32.Alternative Dispute Resolution - Law 34/2002, of 11 July, on services of the information society and electronic commerce", Commentaries on Consumer Protection Legislation, Colex, Madrid, 2011].See there these self-regulation systems („sistemas de auto-regulación: S.A.").

109 Article 31 LMRSF (of Law 44/2002) empowers the Minister of Economy to establish minimum requirements that must be observed by the Customer Service or Department and by the Customer Ombudsman in financial institutions, and the procedure to submit the resolution of claims. To implement this Law 44/2002 provision, has been issued the Ministry of Economy Order ECO 734/2004, dealing with the Customer Services and Departments and the Customer Ombudsman of Financial Entities.

Spain, the National Stock Exchange and the Directorate General of Insurance and Pension Funds, respectively, which are intended to protect the rights of users of financial services in the field concerned (Article 23)[110], without detriment to the use by users of financial services of other systems of protection under current legislation, especially arbitration (and consumer arbitration) regulations.

- Article 31 LMRSF (of Law 44/2002) empowers the Minister of Economy to establish minimum requirements that must be observed by the Customer Service or Department and by the Customer Ombudsman in financial institutions, and the procedure to submit the resolution of claims. To implement this Law 44/2002 provision, has been issued the Ministry of Economy Order ECO 734/2004, dealing with the Customer Services and Departments and the Customer Ombudsman of Financial Entities.

b. What is their success rate?

The effectiveness and success related to mortgage or other loans dispute resolution through out-of-court settlements is still low. The same low rate of effectiveness applies to administrative mechanisms for the protection of financial services customers. By filing an individual reclamation to the Customer Service or Ombudsman, the consumer rarely gets the satisfaction of his claim (for example, never could get the bank to remove the floor clause, and far less, to return the amount charged in base to it). And filing afterwards the complaint at the Bank of Spain only makes that the supervisory body issues a report that can be favourable to the consumer but never binding for the bank.

As for arbitration, very few entities have signed the arbitration agreement: as such, solution by extrajudicial means does not cover the large number of affected by the clause. Submission to consumer arbitration by more banks would be necessary to consider this track as a real alternative.

c. What are the issues?

Usually, since out-of-court settlement has been put into place, the issues with regard to mortgage loans have been related to: re-financing, lieu in payment, debt restructuring, and removal or reduction of interest rates or rent (see below).

Other issues related to financial services in general concern commercial abuses. Thus, most of the complaints achieving public schemes of consumer arbitration in Spain are related to fee increases and their amount, and requests of information on the so-called 'preference shares', subordinated debt and other similar products.

8. Are there special bankruptcy courts? What is their role?

Yes. The so-called Commercial Courts ("Juzgados de lo Mercantil"), specific Courts created by the Bankruptcy Act (passed by Law 22/2003, of 9 July, that came into force on 1 September 2004), which regulates the insolvency situations of both, legal entities and individuals. Particularly specialised in dealing with matters related to Commercial Law, including insolvency, are called to ensure the correct enforcement of the new regulation.

These Courts instruct the bankruptcy proceedings (and also hear and deal with other commercial law matters such as unfair competition, intellectual property, publicity, any matter concerning to corporate law, transports, standard contract terms, and the matters assigned to the Court of First Instance in Section 8 of the Arbitration Act when referring to these matters). Under Spanish Bankruptcy Law, the judge competent to hear the case is the judge of the commercial court "in whose jurisdiction is located the debtor's main centre of interests".

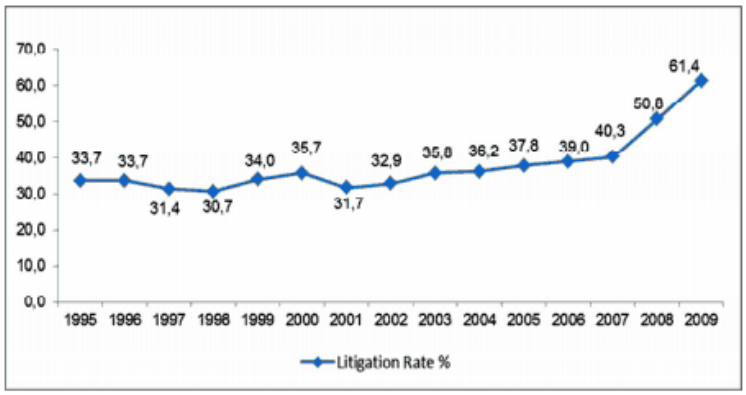
110 In practice, the functions of those Commissioners are assumed by the Claims Service of the respective supervisory bodies.

XIV. Impact of the crisis on litigation

1. Has there been an increase in litigation since the financial crisis?

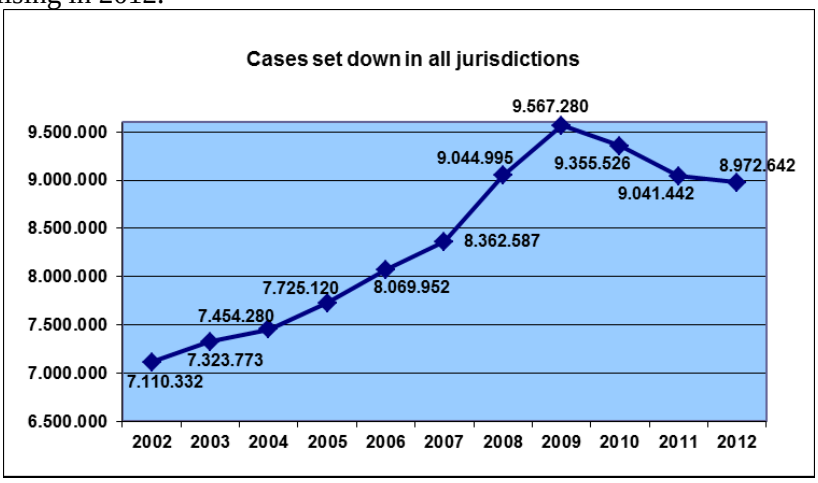
The economic crisis has led to a clear increase in litigation in Spain, as reflected in the Annual Report prepared by the Spanish Judiciary Council. The litigation rate (number of cases filed per 1,000 inhabitants) presented a moderate growing trend from last years of the 1990s to 2007.

Litigation Rate in First Instance Courts. 1995-2009



Elaborated from Spanish General Council of The Judiciary Statistics

However, it rose sharply between 2007 and 2009 before declining in 2010, falling in 2011 (to 2007 levels) and stabilising in 2012.[111]



Source: Spanish Judiciary Council

This year it is decreasing because of the reintroduction (by Law 10/2012, of 20 November) of court fees which had been eliminated in Spain in 1984 – case numbers have fallen by 15%.[112] In absolute terms, the number of cases filed is still very high (around nine million).

a. How many mortgage agreements were challenged in out-of-court or judicial proceedings before and after the crisis?

111 In 1995, were filed, on average, 33.7 cases per 1000 inhabitants; and 39.00 in 2006. In 2007 this litigation rate was 40.00. In 2009, were filed on average 61.4 cases per 1000 inhabitants. Data from the General Council of the Judiciary, The Spanish Judiciary in figures: 2012 / InformeAnual "La Justicia, dato a dato" , Madrid, 2013.

112 As observed by the Statistical Service of the General Council of the Judiciary (CGPJ), in its „Report on a first evaluation of the impact of changes in legal fees", published in Boletín Información Estadística, No. 34, junio 2013.

The challenge before the court on clauses of mortgage contract has been an almost non-existent legal practice until the recent legal reform by Law 1/2013, following the Aziz's judgment. It is due to the fact that challenge in declaratory proceeding had no suspensive effect that could be argued from the enforcement of the contract, as well as hardly possibility of opposition within foreclosure proceedings. Hence there are no statistics on how many mortgage agreements have been challenged in court proceedings (in practice, however, it is now at the opposite extreme, where challenges on grounds of unfair terms are currently massive, figures do not yet exist though).

As regards out-of-court challenge, until the enactment of Law 1/2013, it was not possible in front of Notaries. In addition, there is no published data of how many mortgage agreements have been challenged extrajudicially. The only available data are the claims before the Complaints Service of the Bank of Spain, which only reports that claims relating to credits and loans represents up to the 33.2% of the 14,313 claims submitted to the Bank for all financial matters. It also reports that, in 2012, "a significant increase in complaints related to mortgage loans, a trend that seems to remain similar for 2013".[113]

b. What are the issues challenged? In which legal field?

The issues that have been challenged (even more since the entry into force of the recently passed Law 1/2013 of May 14) are:

- default interest rates (or penalty interest) applied by banks on mortgage loans,
- floor clauses, abovementioned,
- besides to the foreclosure proceedings. Many of them have been dismissed by the implementation of the Law 1/2013 reform, both through the presentation of opposition by the debtor, as ex officio (by its own motion) by the judge.
- and other "minor" challenged issues, thereby unfair terms and abusive practices, also affecting the mortgage payment, are: very high spreads (to compensate the EURIBOR's fall) or benchmarks, abusive increasing fees, abusive repayment systems, and monthly financial obligations imposed by the bank (taking another "product's" shape), and marketing of swaps, clearly linked to the mortgage (for the same amount and signed at the same time).

2. Did the Aziz ruling have an impact on national legislation / legal framework?

The CJEU Judgment in the *Aziz* case (14 March 2013) has had an important impact, not only legal, but also social. It brought about legal reform in procedural regulation. Under the previous rules in the Spanish Civil Procedure Act (CPA), a judge hearing enforcement proceedings was only allowed to evaluate whether the formalities of the proceedings were correctly observed, not the fairness of the provisions of the mortgage loan. Following this judgment, these rules have been amended. The main changes in the CPA are:

- A judge is able and must analyse ex-officio the fairness of the contract in any enforcement proceeding.
- If a court hearing enforcement proceedings finds that the contract contains an unfair term, it must inform and give the parties five days to make a submission on this; and
- if a clause is found to be unfair, then the enforcement proceedings will not continue if the proceedings were based on such a clause. Although the court may stay the proceedings if it deems that a clause is unfair, this court competent for enforcement proceedings is not competent for declaring the unfairness. The parties to the enforcement proceedings must initiate separate proceedings to argue their case concerning fairness or unfairness of the clauses.

113 Banco de España, Memoria del Servicio de Reclamaciones 2012, 2013, p. 37.

The amendment of the CPA will only impact on enforcement proceedings that are pending, but not those that have already concluded. Enforcement proceedings in Spain are likely to be less straightforward from now on, since consumers may allege the existence of abusive terms in the loan with the aim of delaying enforcement. It remains to be seen to what extent the Spanish courts will stay enforcement proceedings if allegations made by a borrower in enforcement proceedings clearly lack any merit.

a. Are there cases before national courts dealing with issues that also arose in the Aziz case?

Yes. In fact, the *Aziz* case seems to have opened the door to undertake action in the field of procedural law when it comes to consumer issues by challenging Spanish procedural rules via the consumer protection provisions granted by European Consumer Law. Particularly, national judges are currently referring several questions to the CJEU for preliminary ruling on the interpretation of the Unfair Contract Terms Directive and the compliance of the Spanish procedural law with the European instrument.

b. What was / is considered an unfair contract term in the national court rulings before and after Aziz?

Before *Aziz*, there was a lack of a proper transposition within the Spanish legal framework of Article 4(2) of the Directive 93/13/EC on unfair contract terms. It led to the Spanish Supreme court to refer the case to the CJEU which gave rise to the case C-484/08, Caja de Ahorros y Monte de Piedad de Madrid.

Law 1/2013, of May 14 on measures to reinforce the protection to mortgage debtors, debt restructuring and social rent, applying the judgment of the Court of Justice of the European Union of 14 March 2013 (*Aziz*) amended Spanish Procedural Law to allow the determination of unfairness, ex officio by the judge or by opposition of the debtor to the enforcement proceedings. On the other hand, the Judgment on Aziz has meant clear support for the possibility of assessing the unfairness by the registrars of property, as public authority. Thus, it opens the door that not only judges are entitled to perform the assessment, but also any public authority without prior judicial ruling may reject unfair terms in consumer contracts.

Following-up Aziz

Shortly after the European Court decided the case, the referring national judge pronounced his judgment.[114]According to the national ruling, the mortgage signed by the complainant contains three unfair terms: 1) the default interest clause; 2) the acceleration clause; and 3) the clause on unilateral quantification of the amount owed.

The judge acknowledges that the default interest clause included in the mortgage contract should be considered unfair and not be applied, resulting in its incorrect calculation. As for the acceleration clause, the contract was agreed for a period of 33 years –396 months. The ruling underlines that the acceleration clause was enforced when Mr. Aziz defaulted on only four monthly instalments, "…0.328% of the amount borrowed". In this regard, the Judgment remarks that:

"it is definitely serious that the debtor has failed to pay four installments, although such failure could be anticipated according to the data at the disposal of the financial institution regarding the assets and income of the consumer(…) very difficult to understand that, taking into account the amount requested as a loan and the agreed

114 Sentencia de 2 mayo 2013. Juzgado de lo Mercantil no. 3 de Barcelona [JUR 2013\139303]. In his ruling, the judge draws attention to three circumstances of the case: a) the value of a property on "just over 194,000 Euros for an apartment a bit bigger than 50 square meters in a neighbourhood of a dormitory town"; b) the awareness by the financial entity on the fact that Mr. Aziz perceives "a single salary slightly higher than 1,100 Euros net per month, determining that as of January 2008 the monthly instalment amounted to 841.64 Euros, having to apply more than the 70% of his monthly net income to the payment of the loan"; and c) that the property was awarded to the creditor for 50% of its appraised value (EUR 97,200.00).

term, the failure of the payments should not be considered serious enough, when they were, in addition, predictable".

Furthermore, according to the national judgment, the seriousness of the defaults must be read in conjunction not only with regards to the percentage of the unpaid debt to a loan designed for very long term, but also with the tools that the financial institution might have available to claim the debt. With the acceleration clause being void, the financial institution could not claim the total outstanding principal amount, but only the unpaid instalments, plus interests.

Finally, the Judge deemed it appropriate and relevant to emphasise the considerations made by the defendant in their closing arguments after the CJEU's Judgment. The defendant raised the question of to what extent the judge feels free to decide on the case in so far as that party considers that the public opinion is representative of some issues not related to the case concerned. More importantly, it also wonders whether the judge has to rule on the nullity of the contract term or rather on the "goodness" of the Spanish mortgage system. The judge acknowledges again the circumstances in which the case unfolds, as well as the relevance – "even emblematic"– of the CJEU Judgment(s).

An important milestone on unfairness after Aziz took place as a result of the Judgment by the Supreme Court on the 9th May 2013 declaring the unfairness of "floor clauses" (analysed before).

c. *Did Aziz have any other impact on national legislation / legal framework (ie. in the field of procedural law)? What are those impacts?*

Yes. It had an important impact on the field of procedural law. For the sake of legal certainty, the Spanish legislator has been entrusted with the obligation of including among the causes for the opposition to the enforcement procedure the abusive status of one or some of the clauses of the mortgage contract. Concerning the declaratory proceedings, it is considered that once the unfairness has been accepted, the effect should be the nullity of the enforcement or, at least, its precautionary suspension.

3. *Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework? Elaborate.*

Yes, the Judgement of the Supreme Court of 9 May 2013 is a milestone in the national legal framework by declaring the unfairness of the so-called floor clauses (the case has been addressed above in Section XIII, §1).

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

Prior to the reform of the Spanish Mortgage Law, judges from the whole Spanish territory have voluntarily started to act on their own motion suspending foreclosure proceedings when they have detected unfair terms. Consequently they have replaced the legislator and took the unusual initiative of not applying the Spanish Civil Procedural Law in order to stop evictions while awaiting a regulatory amendment. Thus, over the course of some months, Spanish judges have been deciding the suspension of foreclosure proceedings while waiting to hear how the CJEU solves the issue at hand.[115]

115 It has been documented in http://www.legaltoday.com/actualidad/noticias/los-jueces-estan-supliendo-al-legislador. See also Cordero Lobato, E., «Control judicial sobre cláusulas abusivas y ejecuciones hipotecarias», Revista Aranzadi Doctrinal, no. 2/2013.

Furthermore, just after Advocate General Kokot issued her opinion on the *Aziz* case,[116] there were a gradual number of suspensions of evictions suspensions by the Spanish courts.

2. Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?

Bankruptcy law, mortgage law and financial supervision regulation are the fields which have experienced a more remarkable change in Spanish law as a consequence of the financial crisis, as it has been discussed throughout this report.

3. What are the changes in particular? Focus on consumer credit and mortgage law.

On 15 May 2013, the amendment of the Spanish Mortgage legislation performed by the already cited Law 1/2013 entered into force. The main amendments introduced by this reform are:

- Suspension of the eviction of families who are at a particular risk of exclusion (Article 1). It is an exceptional and interim measure, which will affect any judicial foreclosure proceedings or extrajudicial sale by which the creditor is awarded the property of the home residence.
- Suspension of the eviction in case of unfair contract terms (Article 7). The new legislation provides the judge with the ability to temporarily suspend an eviction where the concerned consumer claims the unfairness of the contract term(s). In cases where the eviction is motivated by one unfair term, the judge may terminate the process, although the procedure will continue without the application of such contract term. The law also gives similar powers to the notary.
- Default instalments. The reform sets a new minimum quantity of defaults for which the lender may seek enforcement of a mortgage. This minimum has shifted from one to three unpaid instalments.
- Default interest. One of the key objectives of the new text is to put a limit on the default interest that currently stands at rates that may range from 18% to 30%. The reform narrows the charges that the bank can impose on the debtor up to three times the legal interest. Today it would mean a cap at 12%.
- The new law also includes, inter alia, other significant changes in the procedure for the auction and adjudication process of the property. Now the law provides that under no circumstances can the value of the property be less than the 75% of the value stated in the appraisal conducted in accordance with the provisions of Law 2/1981 of 25 March regulating the mortgage market. It also introduces transparency provisions and temporary limits for the design of new mortgage contracts as well as the possibility of nonrecourse debt (dación en pago) under exceptional circumstances.
- Finally, the Law contains in its Annex a Code of Good Practices for financial entities on the feasible restructuring of debts with a mortgage guarantee over the main residence.

In addition, as a temporary solution, the Regional Government of Andalucía enacted a much discussed Decree [117] which authorised the temporary expropriation within three years of the use of houses "in imminent" eviction and if there is a "risk of social exclusion or threat to the physical or mental health of the people". The Constitutional Court of Spain has decided the interim suspension of the application of this Decree, by accepting the constitutional proceedings brought against this measure by the Central Government, which considers the rule from Andalucía "affects the essential content of the right to private ownership, which is a reserved rule to Parliament, establishes a punitive liability regardless of fault principle that is required by the Constitution and establishes a regulation contrary to the equality principle. "

116 Delivered on 8 November 2012.

117 Decree-Law 6/2013, of April 9, on measures to ensure the fulfillment of the social function of housing. It declares the "social interest" of the necessity of housing of those people incurred in special conditions involved in foreclosure proceedings urged by financial institutions or their subsidiaries, or entities of real estate management.

Other initiatives

The Spanish General Council of Notaries has proposed the creation of a body for the control of unfair terms. This body will aim at the creation of a database of all the rulings declaring the unfairness of a term, so that notaries could verify the contract at the time they are required to grant a notarial document. According to the General Council of Notaries, this initiative attempts to address the inefficiency of the Registry for Standard Terms as long as the not all the terms declared unfair are register by the parties in this Registry.

4. *When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

The need for the above-mentioned changes was brought about by the *Aziz* ruling and the social problems entailed in the rising number of evictions in the aftermath of the financial crisis.

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, i.e. with regard to savings?)*

Yes, with regard to the so-called "preferred shares" (known in Spain as "[participaciones] preferentes".

After Spain's decade-long property bubble burst in 2008, savings banks stepped up their marketing of preferred shares as they tried to boost their solvency ratios to meet stricter regulatory demands (and give a better look to their financial statements, since these stocks could be recorded as equity for accounting purposes). Preferred shares were sold to retail investors as equivalent to certificates of deposit, assuring people that they could be repaid immediately or with a couple of days of prior notice. Investors were not informed that, not being bank deposits, they were not insured by the "Fondo de Garantia de Depósitos" (Deposit Insurance Fund). As such, investors were unaware that they were holding unsecured debt instruments.

Nearly one million Spanish depositors, many of them pensioners, poured money into preferred shares issued by their banks after being told by their bank managers that it was a "safe" product that would deliver a good rate of return. According to press sources, Spanish and foreign retail investors sold €30 billion of this (what is now considered toxic) financial product, and have lost a 30-40% of their money, that in many cases represents their entire life's savings.[118]

Marketing of this product was backed by the Financial Supervisor ("Comisión Nacional del Mercado de Valores") and, in the case of bonds issued by banks, was sponsored by the Bank of Spain.

Preferred bonds ("participaciones preferentes") are negotiable debt instruments issued by a company which do not confer equity interest or voting rights. They are perpetual, that is, they do not have a maturity date, and their yield is generally variable, not guaranteed. One of the key features of preferred bonds is that the interest is conditional upon the issuer achieving a predetermined level of profits. It is a complex and risky instrument that can generate high returns, but also losses of the capital invested: it combines the price risk (also called interest rate risk) and the liquidity risk. Like most fixed income instruments, its price is negatively correlated with interest rates. However this potential risk is

118 See El País, The great preferential share swindle, Augost 6, 2012; See Agence France-Presse,"Spanish pensioners pay price of bank share fiasco", March 22, 2013, in http://www.globalpost.com/dispatch/news/afp/130322/spanish-pensioners-pay-price-bank-share-fiasco .

leveraged by the lack of liquidity of the market (that means the lack of marketability of such an investment, which cannot be bought or sold quickly enough to prevent or minimize a loss). The investment was traded in a secondary (and very illiquid) market which was intended to serve institutional investors.

During the boom period, few seriously considered credit risk: the potential loss derived from default and failing to pay due to its insolvency. However, unfortunately, this risk became real with regard to most preferred bonds issuers, the "Cajas de Ahorros" (the saving banks). Thus, those preference share investments quickly became a costly trap, especially after the financial and economic crisis that hit highly indebted countries, like Spain, especially hard where the real estate market bubble burst. As savings banks ceased making profits they suspended the payment of interest on preferred bonds. Further, as the value of the preferred shares plunged it became effectively impossible to resell them. Holders of preferred bonds found themselves holding unsecured debt instruments issued by insolvent entities, which were not paying any interest, without the possibility of selling the bonds.

In addition, savings banks were not allowed to fail according to Bankruptcy Laws. Instead they were bailed out by the Rescue Fund set up by the Spanish Government (the "FROB") funded with tax payers money and with loans from the European Stability Mechanism ("ESM"). The European institutions agreed to lend Spain up to €100 billion to help the country shore up its banks, but insisted, as one of the conditions of extending the rescue funds, that bank customers who bought preferred stock would have to share in (i.e. absorb) bank losses.

We consider that preferred bonds are not inherently fraudulent; but what could be regarded as fraudulent were the means and commercial practices by which they were sold to investors.[119]

Numerous legal cases have been brought by bank clients who allege they were sold risky products as secure deposits and some have succeeded in obtaining their money back. The Spanish Ombudsman's office has received 1,274 complaints over the sale of preferred bank sales since 2011, mostly from elderly bank clients. Additionally it recommended that all banks that received State aid under "universal arbitration" regarding the sale of preference shares. Furthermore, Finance Minister Luis de Guindos said that preference shares should never have been sold to retail investors (savers), while supporting arbitration in case of "misselling" (in which buyers lack the necessary information to fully understand what they were buying) stating that in such cases they would have the possibility to recover the entire investment".[120]

The Spanish government is concerned by the expected volume of lawsuits against preferred bond issuers. Nationalized banks may not be able to assume the cost of these cases without further financing coming from the ESM, which at the end would be more public debt. The government is trying to limit the damages to the nationalised banks sponsoring the resolution of disputes according to arbitration procedure held before the Consumers National Institute ("Instituto Nacional de Consumo"), which is a public agency dependent of the Ministry of Social Affairs. As such, it is a public institution which decides on cases that should be subjected to this arbitration, whose members (note, of an arbitration body) are public officers.

This "institutional arbitration" raises many questions about its articulation, procedures and, above all, the impartiality of the arbitrator. Neutrality of the arbitrator, normally chosen by agreement between the parties in dispute, is an essential feature of arbitration. However, in this case, this is a public

119 The same opinion is maintained in Alvarez, E., The "preferentes" fraud: arbitration or lawsuit ?, available at http://www.spanishsolicitorandlawyer.com/preferentes, 2013.

120 EL PAÍS, 'Guindos dice que nunca se tendrían que haber vendido preferentes a ahorradores', 3 July 2012, available at http://ccaa.elpais.com/ccaa/2012/07/03/galicia/1341308236_157148.html; EL PAÍS, 'Bankia facilitará el arbitraje para titulares de preferentes estafados', 18 December 2012, available at http://economia.elpais.com/economia/2012/12/18/agencias/1355828011_565768.html.

agency, funded by state funds; and the cost of the awards should be paid, at the end of the day, with tax payers' money.[121]

Finally, despite a government initiative to promote arbitration as the means for the resolution of this litigation, judicial means have begun to gain strength, since consumers injured realised that arbitration only provided limited redress. In recent days, a number of judgments have been issued in favour of consumers affected by preferred shares.

121 See Alvarez, E., The "preferentes" fraud, cit, who considers that "the effort of the Spanish Government to promote the use of arbitration to settle the disputes brought by preferred bond holders is an attempt to control the process and limit the damages to the public finances at the expense of retail investors. In short, it is a trap. Retail investors would be better off bringing their cases before the Courts".

CASE STUDIES: NON-EURO COUNTRIES

HUNGARY

Mónika Józon

Preliminary Information

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

In Hungary the terms indebtedness and over-indebtedness are not defined in legislation, jurisprudence or policy. These concepts have a dynamic content that makes it difficult to provide a general definition for research purposes of who should be considered indebted or over-indebted on the basis of the policy measures enacted in Hungary during the past four years. After 2010 there evolved a still ongoing aid process for debtors in severe payment difficulty with several schemes and different criteria of eligibility that continuously refine the borders between different categories of debtors. Thus one can talk of '*debtor mobility'* in terms of the financial risks they constitute on the mortgage market that is difficult to capture in legal theoretical patterns.

Banking practice and central statistics operate with the concept of payment default. Those who cannot pay monthly instalments over more than 90 days are considered to be in payment difficulty. However, being in one or other category of default is not equal to being indebted or over-indebted, since this could mean a temporary inability to pay monthly instalments. The 2013 Consumer Financial Risk Report of the Hungarian Financial Supervisory Authority (hereafter: HFSA) defines the category of *'no problems free*' loans as comprising loans renegotiated, restructured and those with payment delay less than 90 days: thus all loans which may imply any kind of reimbursement problem.[1] Thus, there is no overlap between the actual financial capacity of the debtor to perform under the initial loan agreement and his subsequent status on the 'market of debtors' that often changes not only under the influence of the rescue measures of the state, but also under voluntary debt reassessments between consumers and credit institutions and between the consumers and factoring companies to which the credit institutions sell their receivables.

For this reason one should be cautious in drawing conclusions for research purposes from the official statistical data on the changes in the total value of private debt or on over-indebtedness. In addition, different state institutions (such as the National Bank of Hungary, Central Statistical Office, HFSA) operate with different criterion in assessing the developments on the 'market of debtors'. Comparison of the assessments issued by the Central Statistical Office revealed that data concerning the same year can be different depending on the criteria of assessment employed or the focus of the assessment. Last but not least, in assessing who are the most affected debtors another difficulty comes from the focus of the policy on certain categories of consumers or types of loans, which is reflected also in the methodology of the official assessments. All these made it difficult during the research to offer a full picture on the evolution of the situation in Hungary.

1 https://felugyelet.mnb.hu/data/cms2409345/fv_kockazati_jelentes_2013_II.pdf

2. *Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?*

The global financial crisis reached a consumer credit market in Hungary that was not balanced by a consumer-focused approach on the provision of financial services to private persons, although the market was not fully competitive to cure its failures. Thus the concept of vulnerable consumer was not defined by law. In fact, even the ex post judicial responses to this legal framework were usually built on the traditional principles of contract law (such as equality of the parties, contractual freedom) almost ignoring the tools available under the EU law on unfair contract terms, except from the developments in the case law from the year 2013 onwards. Therefore, most of the court decisions did not contain consumer policy arguments emphasising that the debtor is a weaker party who needs special protection under the law.

Acknowledgement of the far-reaching liberal regulatory background of the credit market at the time of the consumer loan boom and the subsequent, mostly ineffective judicial responses to the crisis is central for understanding the aim, function and effects of the regulatory measures adopted since 2010 in Hungary. The year 2010, often referred to in this Report, is the turning point in the Hungarian regulatory approach in terms of abandonment of this liberal policy. However, even the new regulatory approach, strongly committed to protecting debtors, does not employ real consumer policy arguments, or typical consumer law terminology. The new regulations are enacted along domestic policy and regulatory values, aimed to address, above all else, the macroeconomic and social consequences of the inability of large groups of private persons to repay their loans. These measures, in line with the larger social dimension of the regulatory policy, focus on the 'citizen' in need of protection, rather than the 'consumer of financial services as active market player'. So far, the new Hungarian approach, in place since 2010, has a stronger social dimension rather than a consumer protection aim, which is not pure policy but is also rooted in the weak internalisation of consumer policy into the domestic legal thinking and in the conservatism of the judicial culture in the field of contract law.

3. *Is the term "poverty" or "low-income consumer" defined in the national legal order?*

A further consequence of the liberal regulatory approach is that neither legislation nor banking practice has devoted any attention to debtor poverty at the time of the credit boom. Banks did not differentiate between low income and high income clients and no regulatory framework was in place on consumer creditworthiness. Under the new regulatory approach poverty is central element of the debtor rescue packages enacted since 2010.

II. Numbers on over-indebtedness

1. *How many consumers are considered "indebted" in the country? (since 2000)*

   a. *How many consumers have mortgage debt?*

The table contains the number of new mortgage loan agreement during 2001-2010[2]:

2001	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009** **2010**
76,319	151,859	196,671	124,216	121,134	148,799	130,655	145,504	55,950 41,584

2 KSH Társadalmi Helyzetkép, 2010, Lakáshelyzet, p. 17.

The tables below contain the number of contract/year, published by the National Bank of Hungary[3].

Mortgage loan for housing purposes, denominated in foreign currency:	**Mortgage loan for non - housing purposes denominated in foreign currency:**
December 2011: 282,381	December 2011: 330,096
December 2012: 227,723	December 2012: 287,407
December 2013: 213,683	December 2013: 287,407

Mortgage loan in HUF (subsidised):	**Mortgage loan in HUF (at market price):**
December 2011: 275,569	December 2011: 201,428
December 2012: 242,032	December 2012: 252,626
December 2013: 234,795	December 2013: 262,263

b. How many consumers have motor vehicle debt?
At end of 2013 the National Bank of Hungary reported 239, 993 contracts.[4]

Contracts in HUF:	**Contracts denominated in foreign currency:**
December 2010: 24,457	December 2010: 163,650
December 2011: 38,741	December 2011: 161,412
December 2012: 104,084	December 2012: 164,892
December 2013: 98,769	December 2013: 141,224

c. How many consumers have other debt (credit card, general consumption)?

At end of 2013 the total number of current account debts was 2,873,920 out of which credit card debts made up 942,404[5].

Current account debts:	**Credit card debts:**
December 2010: 3,083,147	December 2010: 1,007,038
December 2011: 2,907,491	December 2011: 989,064
December 2012: 2,878,349	December 2012: 924,544
December 2013: 2,873,920	December 2013: 942,404

d. What percentage of those "indebted" consumers / households (a, b, c) is:

i. Single / married

ii. With / without children?

iii. With / without work?

iv. Retired?

v. Low-income consumers?

Such information is not available.

2. How many consumers/ households are considered "over-indebted" in the country? (since 2000)

a. How many individual consumers / households are behind with the repayment of (up to 3 months and more than 3 months):

3 http://www.mnb.hu/Statisztika/statisztikai-adatok-informaciok/adatok-idosorok/iii-penzugyi-stabilitasi-statisztikak/a-haztartasi-szektor-reszere-nyujtott-hitelallomany-osszetetele

4 *Id.*

5 *Id.*

According to the assessment of the Hungarian National Bank by end of December 2013 18.8% of households debt was overdue by more than 90 days, where in the case of restructured loans under the different debtor rescue schemes the percentage of payment defaults for more than 90 days amounted to 50.3 %.[6]

i. *General consumption loans including credit card loan*

ii. *Motor vehicle loans*

iii. *Student loans*

iv. *Credit card debt*

v. *Interests*

This information is not available.

b. How many individual consumers / households have initiated bankruptcy proceedings?

There is as yet no law in Hungary on private bankruptcy.

c. How high is the average amount of outstanding debt?

According to the assessment of the Hungarian National Bank the outstanding debt of the Hungarians amounted to 6893.6 billion HUF in November 2013, this being in decline for the first time in the past five years.

d. What percentage of those "over-indebted" consumers / households (a and b)is:

i. *Single / married*

ii. *With / without children?*

iii. *With / without work?*

iv. *Retired?*

v. *Low-income consumers?*

This information is not available.

III. Numbers on evictions

1. How many evictions have there been per year since 2000 (or later if earlier data not available)?

In 2011 a quota system was introduced by the Government to protect consumers in payment difficulty, although the number of evictions was low even before the introduction of the quota. The quota use was 74% at end of 2011, 68% at end of 2012 and 71% during the first three quarters of 2013. During 2011-2013 the financial institutions evicted individuals from only 17,000 properties. The number of evictions is far below the number of the properties purchased by the state or those sold by debtors in payment difficulty. For example, in the first quarter of 2013 only 37 properties subject to eviction by the financial institutions, compared to 425 purchased by the state and 213 sold by the debtors. In the second quarter of 2013 this number evolved as: 58 evicted by credit institutions, 912 purchased by the state and 299 sold by debtors[7].

2. How many evictions took place because of:

6 http://www.mnb.hu/Root/Dokumentumtar/MNB/Statisztika/mnbhu_statisztikai_idosorok/penzugyi-stabilitasi-statisztikak/H34_Tajekoztato_2013_q4_hu.pdf

7 PSZÁF Kockázati Jelentés, 2013 június.

a. *Unpaid mortgage instalments?*

b. *Unpaid monthly rent?*

No such separate data is recorded centrally.

3. *Who are the persons affected (percentage of young people, families, retirees, unemployed, level of education, low-income consumers)?*

Data not available.

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

1. *Is the CCD 2008/48 implemented into national law?*

Directive 2008/48 was implemented in Hungary by Law no. 162 of 2009.

2. *Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?*

Hungary extended the scope of application of CCD 2008/48 to cover mortgages, financial leasing and overdraft facilities. Article 12 of the Law provides special rights on pre-contractual information in case of secured transactions and instead of a general provision on personalised information, a separate annex details the special obligations placed on the credit institutions. Annex 3 contains a form on general information to be provided to the client when a mortgage loan is concluded. However, no mention is made of a right of withdrawal in the compulsory information to be provided in the forms on secured transactions. The assessment of the personalised information-form applicable for secured transactions reveals that the requirements towards the financial institution are less stringent for secured transactions than those listed in the general provisions on consumer information applicable for other types of loan agreements. It does not apply Article 11, the obligation of the credit institutions or the intermediary to provide to the consumer information which allows him to assess whether the loan corresponds or not to his needs and creditworthiness on, to mortgage loans. The personalised information covers only the main characteristics of the loan, its effects on the financial situation of the borrower, the consequences of missed payments, including penalties for default, and information on the termination of the loan and enforcement of the securities. The special treatment of the secured transactions also applies in respect of the compulsory content of the contract.

3. *With regard to the Mortgage Credit Directive Proposal: will there have to be an adjustment of national law if the Proposal is adopted as is? What would be the changes in particular?*

The consumer credit market seems to be overregulated in Hungary as a result of the regulatory reactions of the past years onto the missing or weak legal framework. The fast-tracked and piecemeal regulatory approach causes legal uncertainty and has no deterrent effect. Therefore, the credit market takes the approach that the enactment of the Directive would bring more legal certainty into the market.

4. *How is the national legal framework with regard to the UCT 93/13?*

The UCT Directive 93/13 was implemented into the Civil Code in Article 209/A, whereas Government Order No. 18/1999 provides an open list of unfair clauses. According to the initial wording of Article 209A unfair contract terms could be challenged by the contracting party whose interest was harmed by such a term, which meant that only the consumer could act in its own interest.

Only later did the Kúria (the Supreme Court of Hungary) clarify on the basis of ECJ the case law, in form of a soft law instrument (Opinion 2/2010/VI.28./PK), that the courts should proceed on their own motion with the unfairness test for consumer contracts. The initial version of Article 209A was amended by Law No. III. of 2006 that clarified that such terms are void and cannot be enforced against the consumer and also opened the possibility for organisations established by special law to require the annulment of unfair terms in consumer contracts. In addition, it was acknowledged that nullity of unfair terms has *erga omnes* effect towards all the contracting parties with whom the business entity applies the same contracts. A second amendment of Article 209A occurred in 2009 when the unfairness test was extended to include negotiated terms not drafted in a plain and intelligible way. Moreover, it was clarified that terms relating to the main subject matter of the contract can be exempted from the unfairness test only when drafted in plain and intelligible language.

On March 15, 2014 a new Civil Code entered into force in Hungary, which transposed the UCT Directive 93/13 in Articles 6:102-6:105. However, the new Civil Code did not bring changes in the Hungarian approach on the law relating to unfair contract terms on the basis of the lessons learned from the case law of the CJEU or from the conflicting domestic case law on unfair contract terms law. It seems that the task of realigning the Hungarian law to the letter and spirit of the European law is squarely on the shoulders of the judiciary.

Two remarks are worth making in relation to the function of the Hungarian implementing rules of the UCT Directive 93/13 in providing effective tools for ensuring justice between credit institutions and debtors. On the one hand it is indisputable that Article 209A was not promptly adapted in reaction to the difficulties experienced by the courts arising from the interplay of Article 209A with the provisions of civil procedural law and general contract law in line with the developments in the case law of the CJEU. Consequently, this is why Hungary continues to be, along with Spain, a leading country among the EU Member States in referring questions to the CJEU on various aspects of the UCT Directive. Until 2013 the weak impact on subsequent cases of even those preliminary rulings issued by the CJEU in response to the Hungarian references would have justified greater emphasis on clear positive rules on the role of the courts under the UCT Directive 93/13 in order to pursue the courts to apply the unfair contract terms law on their own motion.

On the other hand, those provisions of Article 209/B that made it possible for the consumer protection authority to play an active role in challenging the fairness of consumer credit contracts were in place since 2006, but the authority did not effectively assume such a task.

Thirdly, since the UCT Directive does not address all aspects of the consequences of finding unfairness, effective enforcement of unfair contract terms law in Hungary was also a result of the lack of any adaptation of general contract law on contract invalidity in line with the unfair contract terms law. Thus, in a strongly positivistic judicial culture such as in Hungary where the courts consider themselves as being primarily bound by substantive rules, one can establish that the lack of clear positive rules on how the courts should proceed in applying the law implementing the UCT Directive significantly contributed to the focus of the lawyers and the courts on general contract law in search for ways to provide contractual justice in the field of consumer credit law in the first years upon the manifestation of the global financial crisis in Hungary. On the basis of the wording of the implementing rules neither the legal profession nor the judiciary acknowledged the potential of the law on unfair contract terms to balance the interests of the parties to the loan agreements.

V. Enforcement of consumer credit contracts

1. What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?

Banking practice is not uniform on the cancellation period of the contract for non-performance by the debtor. The bank will usually terminate the contract after a period ranging from 90-180 days,

calculated from the date when payment was due according to the general conditions and terms of the bank. However, the banks usually try to find a solution with the debtor in payment difficulty, such as reassessment of the monthly instalments, which means the prolongation of the contract.

2. What are the requirements to initiate enforcement procedures against the consumer?

If the bank decides to enforce the contract then it must initiate enforcement at the territorially competent court that will issue an enforcement order upon which the judicial enforcement company may proceed with the enforcement. Eviction is the ultimate solution. The enforcement company is bound by law to act according to the principle of gradualism and proportionality set in Article 7 and 8 of Law no. LIII. of 1994. However, in practice it often happens that the eviction takes place despite the public law measures aimed to protect the debtor due to the fact that another enforcement company commissioned by other creditors may enforce a low value debt against the creditor instead of trying to satisfy the claim from the monthly income or the movable property of the debtor.

The main rule is that judicial enforcement must be done from the amount at the disposal of the debtor; from salaries, payments based on employment or social security insurance; or other regular incomes of the debtor. Only when it is foreseeable that one cannot satisfy the claim from these sources within a reasonably short time can the claim be enforced from any movable or immovable property of the debtor. The immovable property can be sold only if the claim cannot be fully satisfied from other sources or this would require an unreasonably long time. Where the total value of the claims are lower than 1,000,000 HUF the mortgaged immovable cannot be sold even when such claims were secured by the mortgage, except where the debtor did not make use of their right to payment in instalments, granted under Article 52/B. This possibility was only introduced July 2013 by Law no. XCIX.

3. What are the steps of such enforcement procedure?

On the basis of the enforcement order, the enforcer will request the Land Administration to register the enforcement right and will obtain the list of persons who have rights registered in the Land Registry over the immovable property. The Land Administration will also notify the parties and the persons who have registered rights over the immovable of the registration of the enforcement right. Other creditors can join the enforcement procedure within fifteen days by submitting their request to the enforcer. The enforcer establishes the value of immovable property on the basis of tax and value certificates not older than six months and upon the request of either party (creditor or debtor) will take into account the opinion of an expert. It will publish the announcement on the public auction in the electronic registry of auctions within 30 days upon the evaluation of the immovable property.

In case of successful auction, the enforcer will inform the debtor of the result and their right to challenge it within fifteen days. The immovable property will be put at the disposal of the new owner after the lapse of 30 days from the date of the auction, upon payment of the price by the new owner. The debtor has 30 days from the date of the public auction to empty the property and to move out. Where the debtor has not moved out from within 30 days, upon the request of the new owner (to be submitted within fifteen days) the enforcer takes the necessary steps for putting the immovable property at his disposal. The enforcer has fifteen days from the time when the court decision became final to elaborate the payment plan upon which the amount resulting from the auction of the immovable will be shared by the creditors. The creditors will have fifteen days from the receipt of this plan to challenge it in court. The court is entitled to amend not only the part of the plan that affects the interest of the creditor concerned, but also other parts of the plan in order to rectify calculation errors and other mistakes, as well to correct those parts which do not comply with legal requirements.

4. Can the consumer raise substantive objections against enforcement?

Law LIII. of 1994 only establishes rules on when and how to raise the objection on procedural issues, it does not deal with substantive objections.

a. Which ones?

It is common practice that once the bank tries to enforce the contracts, the debtor invokes invalidity of the loan agreement, usually for the reason of subsequent unilateral amendment, the omission of the bank to specify in the contract the THM (Total Loan Indicator) or for lack of valid consent and unfairness.

b. What is the legal effect of such objections?

The Civil Code allows the debtor to ask the court for a declaratory judgement on contract invalidity without ruling on the consequences for the parties of finding contract invalidity. This prevented further contract enforcement.

In 2013 the Kúria established (Pfv. I.20. 728/2013) that the consumer loan agreement which does not contain the number and the amount of the reimbursable instalments required by Article 213(1) (e) of Law CXII. of 1996 is void when this cannot be established by the court (i.e. the nullity is not remediable). As a consequence of nullity of the loan agreement the Kúria also established the invalidity of the eviction and of the sale-purchase agreement on the mortgaged immovable property.

5. Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?

Law no. CXII. of 1996 on the functioning of financial institutions, in force at the time of the credit boom and still applicable at the beginning of the global financial crisis in 2008, specified in Article 210 (3) that interest rates, charges and other contract conditions may be unilaterally amended under the 'conditions and circumstances established by the financial institutions' if the contract makes this explicitly possible in a separate clause. This provision was in place until 8 August 2009. The situation changed only partially in 2009 with the adoption of the Code of Conduct that contains an exhaustive list of situations where credit institutions may unilaterally change repayment conditions. This is a soft law instrument (although in case of noncompliance by the signatory banks the HFSA can impose sanctions) and applies only to agreements concluded after its entry into force.

The Code of Conduct mentions three main groups of events and circumstances, which justify unilateral amendment of the loan agreement by the creditor: a) changes in laws and regulations directly affecting the contracts on financial services and those on the activity of the financial institutions; b) changes in the financial market, and c) changes in the macro-economic environment and changes in the customer's risk rating

The new rules introduced by Law no. LXXXVI. of 2009 (in force as of January 1, 2010) narrowed the far-reaching liberalism which existed before by limiting the possibility of unilateral amendment of loan agreements and financial leasing agreements to the interest rate, charges and costs. Amendment of other contract conditions, including the conditions on unilateral contract amendment is no longer allowed to the detriment of the debtor. However, the creditor can only exercise their right to unilaterally amend the contract when the contract explicitly contains the objective circumstances of such amendment and subject that the creditor had previously established his pricing policy in written. However, the law does not detail what is meant by written form. The conditions for the unilateral amendment of the interest rate were further detailed by Government Ordinance no. 275 of 2010. According to this, unfavourable changes in costs of the creditor connected to its financing sources may also justify unilateral amendment of the contract. Increase in the costs of the financing sources may mean increase in the base interest rate of the National Bank of Hungary, in the inter-bank money market interest rates loan rate, shift of the yield curve of the bonds issued by the Hungarian State or the creditor and the swap yield curve relative to each other and the provable increase of the costs of loan agreements concluded by the financial institution for re-financing the loan agreement.

a. How is the term "unforeseen/unforeseeable events" defined?

The room for the banks to make actual use of the clause on the unilateral amendment of the contract was defined (or at least one can see an attempt for this) by the Highest Court (the predecessor of the Kúria8) in the Partiscum decision Gfv. IX. 30. 211/2011 no. 6 adopted on September 27, 2011 establishing two conditions: a) the actual change in the circumstances must exceed the normally affordable level of the business risk and that the amendment of the contract must be proportional with the effects of the changes in circumstances; b) the occurrence of the change and its actual effect on the interest rate, charges and costs should not be logically foreseen even by a professional market player.

b. If adjustment is possible, what are its legal effects?

The unilateral adjustment is binding for both parties to the credit agreement.

6. Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?

7. Do the banks use private companies that deal with the recovery of debts with the result that legislation on consumer protection doesn't apply anymore?

If the bank decides to terminate the contract, the loan is usually offered for purchase by a factoring company that initiates judicial enforcement upon unsuccessful attempts to obtain payment from the debtor. It takes around six months from the time of non-payment until the credit institutions sale the receivable to a factoring company. Before the factoring company starts the enforcement procedure, the debtor still has the chance to reach an agreement with the factoring company on partial payment, or upon agreement with the factoring company it may sell the mortgaged immovable.

VI. National legal framework applicable for over-indebtedness

1. What are the possibilities for consumers in case they are considered "over-indebted"?

Debtors in payment difficulty may choose between making use of the possibilities of debt reorganisation available from the lending bank or to join one of the aid schemes introduced by the Government after 2010. These are:

- Reconversion of the loan contracted in foreign currency into HUF
- Final payment of the debt
- Exchange rate ban
- Purchase of the debt by the state

a. Is there the possibility for the consumer to reorganise debt or obtain debt relief?

i. How are the terms re-organisation and debt relief defined?

These terms are not defined by law. The regulatory measures adopted to assist the debtors in payment difficulty are strongly policy driven, reflected also in the drafting style. These measures are often revised, thus one can state that for the moment the two concepts have a dynamic content, making difficult any generalisation.

ii. What are the requirements for re-organization and relief?

Each debt reorganisation and relief scheme has its own conditions of eligibility.

Although no central data is available on voluntary debt restructuring, according to the Hungarian Banking Association this is widely practiced since the impact of the global financial crisis on the

8 Kúria is the name of the Hungarian highest court.

Hungarian credit market. Credit institutions settle the reorganisation scheme according to their own policy.

Final mortgage repayment was launched in the autumn of 2011 as the first debtor rescue measure. Debtors having loans in foreign currency had the possibility of repaying the loan at once (during the period of 2011-2012) at a fixed exchange rate set by law, 180 HUF/CHF for loans denominated in Swiss Francs and 280 HUF/EUR for loans denominated in euros. Under the following conditions of eligibility, the scheme was available under Law CXXI. of 2011 for mortgage loans for housing purposes and mortgage loans for free use:

- The exchange applied by the banks was not higher than the new fixed exchange rate,
- The loan was mortgaged with an immovable located Hungary,
- The banks did not terminate the contract for non-payment of the debt until June 30, 2011,
- The debtors submitted a written request for final payment before 31 December 2011,
- Final payment to be rendered within 60 days from the submission of the application by the debtor.
- Final payment of other transitory loans or payment delaying loans.

After April 2012 debtors could convert foreign currency loans in default for at least 90 days into HUF facilities, with the simultaneous write-off of 25% of their entire debt, subject to the condition that the value of the mortgaged immovable properly was less than 20,000,000 HUF and its was not yet subject to eviction. Law XVI. of 2012 set the deadline of August 31, 2012 for the credit institutions to convert existing loans denominated in foreign currency into HUF at the average exchange rate of the National Bank of Hungary during the period of May 15, 2012 –June 15, 2012. The credit institutions were not allowed to charge the debtors with extra costs and fees for the reconversion of the loan into HUF.

The exchange rate ban was introduced in 2012 and involves for debtors the possibility of a five year period (May 2012- May 2017) to reimburse the loan at a fixed exchange rate (180 HUF for 1 Swiss Franc; 250 HUF for 1 euro and 2.5 HUF for 1 Japanese Yen). The debtors are relieved of the interest rate for the amount above the fixed exchange rate. This is taken over by the state and the bank concerned. They reimburse only the capital for this remaining amount, according to the rules on the pool account concluded with the creditor bank. The difference between the actual exchange rate and the fixed exchange rate accumulates on a pool account, which constitutes a HUF based loan.

After five years the debtor will start paying the initial loan at the actual exchange rate and in addition to this he will reimburse the debt accumulated on the pool account. The amount to be reimbursed cannot be higher than 15% of the last instalment paid by the debtor before the termination of the interest rate ban, including the interest rate and other costs of the loan. The period of reimbursement of the amount accumulated on the pool account cannot be longer than the period of the initial loan plus 30 years.

Law LXXV of 2011 established the following criteria of eligibility under this scheme:

- No longer payment delay than 90 days,
- No participation in other debtor aid program,
- The loan expires before December 31, 2014,
- The commercial value of the mortgaged immovable established by the credit institution at the time of contract conclusions was no more than 30,000,000 HUF,
- Where the mortgaged immovable property is under more mortgage loan obligations then the less than 90 days payment delay applies to all mortgages. The mortgaged immovable is not yet subject to eviction.

iii. How many consumers have had debt reorganised?

Until August 2012, when the program on the conversion of foreign currency denominated loans into HUF ended, HUF 23 billion worth of defaulted foreign currency loans were converted, amounting to a 4% participation rate. Thus this program did not have any measurable impact on the NPL rate.[9]

During 2011-2012, 169,256 persons with loans in foreign currency made use of final mortgage payment and 23% of the performing foreign exchange loans was repaid[10].

Until 30 April 2013 more than 158,000 contracts were signed for the repayment of the loans at a fixed exchange rate. For nearly 150,000 of these cases a pool account was also opened. This means that 35% of the eligible consumers joined the program on exchange rate ban. Loan agreements protected by an exchange rate barrier represent more than half of restructured mortgages.[11]

Until mid-2013 11.6% of the loans granted to households were voluntarily restructured by banks upon agreement with the debtors. 95% of these are property-secured loans and 90-92% of the restructured portfolio comprises foreign currency mortgages[12].

iv. How many consumers have obtained debt relief?

Only the value and cost of various debt reliefs is known. Thus, those persons who joined the scheme have been relived from paying back 11.1 billion HUF. The cost of this scheme for the government and financial institutions is on average nearly 74,000 HUF per contract.[13]

b. Is there a possibility for consumers to attain discharge of debt (Restschuldbefreiung) within bankruptcy proceedings?

There is no private bankruptcy in place yet in Hungary. A draft law is under consideration.

i. How is discharge defined in the national context? (Is there a definition?)

ii. If discharge is possible, after how many months/years is it possible?

iii. If discharge is possible, what are the requirements for discharge?

Not applicable.

c. What are the requirements for initiating bankruptcy proceedings for consumers?

It is not the case in Hungary.

d. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

It is not the case in Hungary.

e. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can take recourse to?

Law No. CLXX. of 2011 provides the solution for HUF and foreign currency debtors in default for over one year to have their debts and immovable purchased by the state. The National Asset Management Company (NAMC) purchases the mortgaged immovable property at a discount price from the credit institutions. After this the credit institution discharges the debtor from the debt. The immovable properties are bought by the state at a price of 55% (in Budapest and cities) and 35% (villages) of their commercial value as established in the mortgage agreement. When there is no such

9 PSZÁF Kockázati Jelentés, 2013 június.

10 *Ibid.*

11 *Ibid.*

12 *Ibid.*

13 PSZÁF Kockázati Jelentés, 2013 június.

value established in the agreement then the commercial value established at the moment of the mortgage conclusion is taken into account. The home of the debtor unable to repay the loan will be purchased by the state upon the consent of the creditor bank. The NAMC acts in the name of the state and acquires the immovable which will be later used directly by the NAMC for renting purposes. NAMC can also decide to transfer the immovable into the local social hosing asset of the local authorities, or to propose it for sale.

The following criteria must be fulfilled by debtors to be eligible under this scheme:

- The debtor or persons belonging to his household must be in social difficulty,
- The permanent place of residence of the debtor was on September 28, 2011 and subsequently is in the immovable offered by the bank for purchase to the state,
- The debtor does not have another housing possibility,
- The immovable property was mortgaged before December 30, 2009,
- There is no other security in place for the loans secured by that immovable property,
- The commercial value of the mortgaged immovable at contract conclusion was no more than 20,000,000 HUF in Budapest and other cities, and no more than 15,000,000 HUF in other areas,
- The value of the mortgage loan was not higher than 80% of the value of the mortgaged immovable and 100% in case of loans secured by the state, but not less than 25% of the value of the immovable.

According to the Financial Risk Report of the HFSA,[14] of the quota available until the end of 2012 (8,000 properties) only 1,970 homes were offered by the bank for purchase by the state, and only 600 were actually purchased. The NAMC could have purchased 13,000 properties until the end of 2013 having been allocated HUF 33 billion for this purpose. Considering that the current budget enables the NAMC to buy 25,000 properties until the end of the program and that the number of contracts in default for over 90 days was 195,000 at mid June 2013, the NAMC can serve as solution to a maximum of 12.8% of the non-performing debtors.

Lastly, it should also be mentioned that Law no. XXV of 1996 makes it possible, at least in theory, for both the creditor and debtor to ask the territorially competent local public authority to render the debt of the consumer. This procedure is available to those debtors who did not react or did not pay the debt upon notification from the enforcement company and 60 days lapsed since receipt of the notification, or for those who acknowledged the debt but did not pay within 60 days. This procedure is a non-adversary court procedure conducted by the territorial competent court which will point out a financial administrator who will take the measures aimed to satisfy the claims of the creditors. This short (30 days) procedure may also contribute to the development of the social housing asset of the local communities, subject that the local public administration has enough funds to assist citizen struggling with payment difficulties.

2. Is there a national legal or policy framework for avoiding evictions?

In 2011 the Government put in place a home protection scheme for over-indebted persons through state acquisition of consumer debts (presented at Section V. 1. b). It also set up a quota for evictions, which cannot be exceeded by the credit institutions. Under the scheme on state acquisition of mortgaged immovable the state buys the debts of those persons who are not able to repay the loan, subject the conditions of eligibility set by the law.

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (ie. debt relief)?

14 PSZÁF Kockázati Jelentés, 2013 június.

Under the state-purchase scheme of mortgaged houses the persons affected may stay in their homes if they agree to the payment of rent. They also have the possibility to repurchase the home at a later date. At the moment when the NAMC concludes the contract with the debtor, a repurchase right is registered in the land registry in favour of the previous owner, i.e. the previous debtor. The former owner can make use of this right within 60 months. This right applies even when the immovable property becomes part of the social housing system of the local public authority. The repurchase price will include the acquisition price of the immovable by the state, the basis interest rate of the Hungarian National Bank, the value of investments made over the time by the NAMC, plus the value of the loan paid at the time of acquisition by the state, instead of the debtor.

If the debtor fulfils the conditions of eligibility established by law and the immovable property is subject to eviction the financial institution may request the suspension of the evictions procedure. Where the mortgage loan agreement allowed the sale of the mortgaged property without a court procedure, via public auction, then the financial institution will stop the procedure. The suspension will end if the NAMC decides not to purchase the mortgaged home. At the time of conclusion of the sale-purchase agreement on the mortgaged immovable, the NAMC will conclude a rent agreement with the debtor or other persons appointed through an open competition. Subletting is forbidden by law.

b. Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

No information is available on such practices of the credit institutions.

VII. The regulation of credit bureaus

1. How many credit bureaus are there in the country?

In Hungary there is only one credit bureau in place, the BISZ Zrt.

2. Are the credit bureaus public or private?

BISZ Zrt. is a private law entity, a public limited company set up by banks.

If there are both public and private credit bureaus:

a. How many credit bureaus are public and how many are private?

In Hungary only a private credit bureau is in place to date. However, according to recent news it is envisaged the transformation of BISZ Zrt. into a fully state owned institution.

b. Do the public and private credit bureaus have different functions and / or procedures? Are they concerned with the same data?

3. How are credit bureaus compensated?

The credit bureau does not receive public financing, it a profit oriented public limited company. The financial institutions pay fees for the services of the BISZ Zrt.

4. How do the credit bureaus collect data?

The Central Credit Information System (CCIS) administered by BISZ Zrt. is a self-contained database, jointly operated by over 450 financial institutions and banks in Hungary. Information sharing is mandatory according to Law CXXII. of 2011. For this purpose BISZ Zrt. concludes a Credit Information Provision Agreement with the credit institution.

5. In what do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

There is no specific cooperation in place between the Central credit bureau and the data protection agency. However, the BISZ Zrt. must comply with the requirements of Law CXII of 2011 on informal self-determination and freedom of information.

6. What data is collected by credit bureaus?

BISZ Zrt. records both positive and negative data on consumer credit, including information on credit agreements, default, bank card fraud, rejected applications for fraud.

7. Who are the users of credit bureaus?

BISZ Zrt. provides data to credit institutions which have submitted the data for purposes of data maintenance and to those subscribing to credit history information. It is obliged by law to provide data to the National Bank of Hungary.

(Over-) indebtedness of consumers

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country? Elaborate.

The mortgage loan subsidy scheme introduced in Hungary in 2001 determined that the boom in the construction market that lasted until the end of 2008. During the nineties the number of houses constructed annually was below 20,000 which, owing to the lack of a social housing system in Hungary, could not satisfy the far reaching high demand for homes. For this reason in the period between 2004 and 2009 the number of homes constructed annually increased to 40,000.[15] This has also to do with the Hungarian paradigm that one must own the home. Around 90% of the housing asset of Hungary is therefore under private ownership.

2. What is the relation between housing prices and over-indebtedness?

a. How have housing prices developed since 2000 (or later if earlier data not available)?

From the FHB House Price Index for the period of 1998-2009 show that over the period under assessment housing prices increased by four times their original value, which means an average yearly increase of 13.2 %. The study of FBH identifies major stages in the developments of the housing prices[16]:

1998-2000: significant increase in nominal and real prices of houses

Real estate prices increased by 132% compared with the income of private persons by 46%. The supply side of the housing market could not satisfy the demand generated by the increase in income, which caused the increase in prices. Housing construction was stagnating. Only 20,000 - 30, 000 new homes were built annually. Housing credit was still negligible due to the high level of interest rates.
2001-2003: housing prices continued to increase

The rise in prices continued at a lower rate (60%) over the coming three years with an annual increase of 11%. By the introduction of the housing subsidy program, in the period of 2001 and 2003 the interest rates felt behind the interest rates of the market, with the consequence that the market of new houses started rising by 50% annually.

2004-2007: credit boom

15 KSH Társadalmi Helyzetkép 2010, Lakáshelyzet, p. 11 (Official publication of the Central Statistical Office)

16 KSH Társadalmi Helyzetkép 2010. Lakáshelyzet

This period can be characterised by far smaller increases in housing prices than before and a decline in real value of the house prices started in 2005. In 2004 the housing subsidies program came to an end and the house building market started declining. However, high level of supply on the credit market continued to cause a high level of demand for houses. It is worth recalling a comment on that period*:* "the majority of households, suffering the 'money illusion' of being unable to distinguish nominal from real values, scarcely perceived this depreciation at the time, and even if they did, then presumably they did not believe to be a long effect".[17]

2008: fall in housing prices

In the second quarter of 2008 house prices started falling. The composition and quality of the supply are identified as one significant reason of the fall in prices. Investors began to build large housing estates and the quality of homes changed in favour of functionally minimal, low quality homes. In this period a significant number of first time owners started selling their houses, which pushed down transaction prices.

According to a recent study published in 2013, one can notice a steep fall in the construction of new houses. The number of new houses built fell back to the level between 1998 –2000: in 2011-2012 less than 2,000 houses were built.[18]

b. How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available?

3. Has there been increased access to mortgage credit? In which way? Was access to consumer credit facilitated through legislation? Has access to credit become more restricted since the crisis?

During the years before the start of the global financial crises the market for mortgage loans was facilitated by state subsidy schemes on mortgage interest rates. A study published in 2005[19] assessed the net value of mortgage subsidies in 2002-2004 at 50-70% of the loan. The same authors mention that in 2004 the upper 20% of households in the income distribution received 60% of the total subsidy and that the subsequent cut of subsidies did not have significant effect on the mortgage market, because the market of subsidized HUF loan was taken over by the foreign exchange denominated loans. According to data from the Central Statistical Office the numbers of new foreign currency denominated mortgage loan agreements were 146, 000 in the period of 2005-2007, 146, 000 in 2008, 56,000 in 2009 and 42, 000 in 2010. [20] Due to the new rules on creditworthiness, enacted since 2011, access to mortgage loans denominated in foreign currency is subject to earnings in the currency of denomination. Thus, today is far more restricted the access to mortgage loans in foreign currency than at the time of the credit boom.

4. What is the relation between employment and over-indebtedness?

a. How many per cent of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when over-indebtedness arose?

According to the statistics of the Hungarian National Bank, 87% of housing mortgage loans and 89% of the foreign currency loans were contracted by families where at least one person is employed. In case of HUF loans this is 86%. Falling income is considered the most common reimbursement risk in

17 Op. cit., p. 7.

18 L. Kovács, A devizahitelek háttere, Hitelintézeti Szemle 2013. Tizenkettedik Évfolyam, 3. Szám, p. 184.

19 J. Hegedűs, E. Somogyi, Evaluation of the Hungarian Mortgage Program, in J. Hegedűs, E. J. Struyk (eds.) Housing Finance: New and Old Models in Central Europe, Asia and Kazakhstan, 2005, pp. 199-202). pp. 177-208.

20 KSH Társadalmi Helyzetkép 2010, Lakáshelyzet, p. 12

case of mortgage loan for housing purposes.[21] The study also stresses that almost 40% of the debtors belonging to the low income category struggle with payment difficulties. This amounts to 45% in case of loans denominated in foreign currency and 35% for HUF loans. In case of foreign currency denominated loans more than 30% of the inactive persons could not reimburse the loan or could reimburse with delay, whereas in case of HUF loan this was 20%.

Unemployment increased in Hungary starting with the fourth quarter of 2008 until the third quarter of 2010 (7.9% in 2008, 10 % in 2009, 11.2 % in 2010) followed by a slight fall, but even so it was higher than before the crisis.[22] Between January 2011 and January 2012 the unemployment rate stagnated (11.0%). In 2012 it was 12%.[23] According to Eurostat statistics the largest decrease within the EU was registered by Hungary last year, from 11.2 % to 8.3 % between January 2013 and January 2014.[24] However, this positive development is to a large extent the result of the introduction of the public employment scheme since 2011. This had improved the financial situation of a significant number of households, but it may not have significant impact on over-indebtedness.

At the time of the credit boom gross wages of full time employed people grew in Hungary by 8-9% in the period of 2005-2007, whereas the real value of the earnings was 40%. The table contains the monthly average earnings of full time employees during the period of 2008-2013, based on data published by the Central Statistical Office.

Year	Gross earnings in HUF	Net earnings in HUF	Real earnings
2009[25]	Increase by 0.5 % to 199,837	Increase by 1.7% to 124,116	Decrease by 2.4%
2010[26]	202, 576	132, 628	Increase by 5.8%
2012[27]	Increase by 4.6% to 223, 000	Increase by 2.0% to 144,000	Decrease by 3.3%
2013	Increase by 6% to 226,600	Increase by 6 % to 148,500	Increase by 2.6 %

Thus one can notice a decrease in real earnings after 2008 in comparison to the period when most of the loans were contracted.

5. *Non-EURO countries: Did national monetary policy play a role in consumer credit and mortgage agreements?*

Yes, it did play a major role in Hungary. Details are provided under Section 6.

a. Are/were foreign currency loans common?

Whereas foreign currency denominated loans were the exception in 2004, their share rose to 90% of the new loan agreements concluded in 2008.[28] There are two main reasons for such developments in consumer preference: a) increase of the interest rate for HUF loans compared to more favourable

21 A Hitellel Rendelkező Háztartások Szociális Jellemzői, in Statisztikai Tükör, V. évfolyam, 77. szám.

22 KSH: A válság munkaerőpiaci következményei, 2010-2011 első félév, p. 4 (http://www.ksh.hu/docs/hun/xftp/idoszaki/pdf/valsag.pdf)

23 http://www.ksh.hu/docs/hun/xftp/idoszaki/mo/hungary2012.pdf

24 http://epp.eurostat.ec.europa.eu/statistics_explained/index.php/Unemployment_statistics

25 http://www.ksh.hu/docs/hun/xftp/idoszaki/mo/mo2009.pdf

26 https://www.ksh.hu/docs/hun/xftp/idoszaki/mosz/mosz10.pdf

27 http://www.ksh.hu/docs/eng/xftp/gyor/jel/ejel21401.pdf

28 J. Hegedűs, "Unorthodox" housing policy in Hungary: Is there a way back to public housing? to be published in The Future of Public Housing: Trends in the East and the West (eds):Jie Chen, Mark Stephens, Joyce Yanyun Man, Springer 2013

interest rates for loans denominated in foreign currency and more attractive reimbursement characteristics of the foreign currency loans compared to those offered on the loan market in HUF.

A recent study[29] identifies another incentive (the lower reimbursement burden) that made the foreign currency denominated loans more attractive especially for young families who were the major users of these loans. However, as the author emphasises, the lower reimbursement burden of Swiss Francs was counterbalanced by the continuously changing exchange rate of the loan capital; whereas the initially higher reimbursement burden in HUF loans developed into lower at the end of the contract period due to the inflation of the loan capital. It seems that the consumers have assessed these offers mostly upon their short term effects onto their budget and not in the long run.

Upon the impact of the financial crisis on the debts denominated in foreign currency and subsequent regulatory responses adopted after 2010, foreign currency denominated loans lost their popularity. Today consumer access to foreign currency loans is restricted by law. Those who do not have earnings in foreign currency do not have free access to foreign currency loans. In addition, the government is strongly committed to introducing further measures for the transformation of existing foreign currency denominated debts into HUF debts.

b. What are the foreign currencies in which loan agreements were concluded?

The Swiss Franc was the most preferred currency, followed by the euros.

29 L. Kovács, op. cit.,p. 184.

The table below contains the value in billion HUF of different types of foreign currency denominated loans compared to loans in HUF

	Housing loan in HUF	Housing loan denominated in CHF	Housing loan denominated in EUR
2003/ January	46.9		
2004/ January	47.7		
2005/ January	13.5	10.9	0.3
2006/ January	10.8	23.3	0.6
2007/ January	10.1	42.1	0.2
2008/January	8.6	53.6	0.2
2009/January	7.5	12.5	15.9
2010/January	4.2	2.6	7.6
2011/January	11.3	0.2	0.2
2011/February	12.1	0.3	0.3
2011/March	16.0	0.6	0.1
2011/April	15.0	0.5	0.2
2011/May	18.1	0.3	0.1
2011/June	19.8	0.4	0.1
2011/July	18.1	0.3	0.1
2011/August	19.4	0.8	0.0
2011/September	17.3	0.5	0.0
2011/October	15.9	0.1	0.1
2011/November	22.6	0.0	0.2
2011/December	40.6	-	0.4
2012/January	61.4	-	0.1
2012/February	37.2	-	0.0
2012/March	11.9	-	-
2012/April	10.0	-	-
2012/May	11.9	-	-
2012/June	11.2	-	-
2012/July	11.8	-	-
2012/August	10.8	-	-
2012/September	10.0	-	-
2012/October	9.5	-	-
2012/November	9.7	-	-
2012/December	8.6	-	-
2013/January	8.3	-	-
2013/February	7.7	-	-

c. *Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?*

In Hungary the percentage of indebted consumers with foreign currency denominated loans is higher than those in HUF. In March 2013 the NPL rate of forint mortgages is far lower (12.1%) than that of foreign exchange loans (20.2%).[30]

6. *Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?*

Macroeconomic circumstances played a large role in the development of the consumer credit market in Hungary. These can be classified in four main categories:

- Unfavourable developments in the domestic monetary and fiscal policy at the beginning of 2000 causing high level of interest rates for loans in HUF, whereas the Hungarian potential for economic growth was low.
- Unrealistic and inconsequential political commitments and communication related to Hungary's accession to the Eurozone generated unrealistic hopes for banks and customers that in two to three years Hungary would join the euro and thus the currency risk may be short term. However the estimated date of Hungary's accession to the euro never became reality.
- Market failures and regulatory failures of the public housing sector in Hungary were also a major factor leading to over-indebtedness. Hungary does not have a social housing system, more the 90% of the houses and flats are in private ownership. Before the nineties the offer on new houses and flats was far behind demand. The state aid schemes implemented after 2000 promoted the construction and acquisition of new homes in Hungary. However, the aid scheme distorted the housing market instead of redressing it.
- Banking products such as consumer loans in Swiss Francs were introduced in Hungary especially by foreign banks, such practices not being practiced at the mother companies. Furthermore, the mortgage loan market was not of the oligopolistic nature that would have created a need for follower-attitude among the banks. However, most of the banks have realigned to new products. Banking specialists recall from that period the pressure they had from mother companies demanding high profit targets from their Central-Eastern European subsidiaries that pushed many banks into risk competition.

IX. Micro-economic risk factors for over-indebtedness (consumer behaviour).

1. *What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)*

In Hungary most of the loans were contracted for housing purposes (reasons explained under chapter IV.) and daily expenditure (current account loan).

2. *How many credit agreements do consumers conclude on average?*

According to estimates made on the basis of data available in the KHR system, on December 31, 2012 the number of consumers having loans was 4,798,398 whereas the consumer loan contracts per capita amounted to 1.750604.

3. *Was/is the housing market in the country based on rent or ownership?*

More than 90% of housing assets in Hungary is in private ownership. This high percentage of housing ownership is strongly related to the missing social housing system in Hungary and to certain cultural attitudes. Private renting is highly expensive in comparison to the average income of the Hungarians,

30 PSZÁF Kockázati Jelentés, 2013 június.

since supply is far behind the demand. Owning a house or a flat is traditionally perceived as stability and wealth, therefore Hungarians prefer to own their homes.

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if data available)?*

In Hungary one can speak of the mortgage market in the true sense only starting from 2001 when Law XXX of 1997 was enacted. Previously, the number of mortgage agreements was insignificant. Even in 2007 the number of households mortgaged for housing purposes was only 21.4%, whereas the mortgages for other purposes were 5.7%. The framework law, Law XXX of 1997 established the conditions of mortgage lending and the institutional requirements on the functioning of the mortgage banks, including rules on the issuance of mortgage letter. The Hungarian regulation of the mortgage market was built upon the German model. Once the institutional framework was in place the when the Government launched in 2001 the interest rate subsidy scheme. These two policy measures create favourable conditions for the development of the mortgage market in Hungary.

Before the financial crisis the mortgage GPD ratio was 2% in 2003, 13% in 2006 and 13% in 2007, whereas in 2006 in the EURO zone this was 50% and in the USA around 80%.[31]

A value (Billion HUF) based on central data is also available on the development of the mortgage market in the period of 2001-2009. According to the statistics of the Hungarian National Bank the stock of household mortgage loan evolved as follows:

In the period between 2001 and 2005 the value of housing mortgages contracted in HUF increased from nearly zero in 2001 up to 2000 billion HUF in 2005. Only in 2005 did the foreign currency denominated mortgage market appear. However, the value of these loans only slightly exceeded 2000 billion HUF during the period of 2005-2009.The total value of housing mortgage loans registered its highest values (close to 7000 billion HUF) in 2009. In 2007 this was slightly above 4000 billion HUF.

5. *How many indebted and over-indebted consumers have credit card debt?*

No central data is available.

   a. *How high is this debt?*

The net value of the credit card debts in the period of 2009 -2013 evolved as follows:
June 2009: 75,25
June 2010: 165,350
June 2011:173,716
June 2012: 179,045
June 2013: 178,299
The figures are provided in billion HUF.

   b. *How long does it take consumers on average to repay credit card obligations?*

There is no central information on this matter. According to banks, the usual consumer habit is that credit card debtors delay repayment of such debts.

6. *How many per cent of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?*

The default rate of overdraft facilities is 10%.[32]

31 J. Király, M. Nagy, Jelzálogpiacok Válságban: Kockázatalapú verseny és tanulságok. Hitelintézeti Szemle, 2008, Hetedik Évfolyam, 5. Szám, pp. 451-480.

32 PSZÁF Kockázati Jelentés, 2013 június.

a. *How high is this debt?*

The value of credit overdraft debts was 919,689 billion HUF in June 2013.

b. *How long does it take consumers on average to repay overdraft facility debt?*

Interview conducted with the BISZ Zrt. revealed that based on the data available on credit history, the average time to repay an overdraft facility is around 1 year.

7. *Is there a relation between the length of the credit obligation and over-indebtedness?*

a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*

The problem of over-indebtedness, meaning that the persons' repayment ability exceeds their income and the value of their mortgaged immovable property, is more acute for those having consumption loans than in case of mortgage loans contracted for housing purpose. In many cases both loans are secured by the same mortgage.

b. *How long are the time periods for which consumers took on credit and mortgage obligations? Is there a difference in data from before and after the crisis?*

Mortgage loans were contracted by banks for shorter periods in Hungary than in Western Europe. Usually they range from ten to fifteen years.

c. *What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?*

There is no specific information available on the relationship between the length of the contract and payment difficulties. However, according to information provided by the Association of Mortgage Banks, payment difficulties usually arise during the first five years of the contract. No differences can be noticed according to the banks between long and short term loans concerning default within the same type of loan. However, the differences in default ratio between long term mortgage loans and shorter consumption or personal loans reveal that non housing loans are more risky than mortgage loans, since their debtors are more often in payment difficulties.

X. Relation between income and (over-)indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

In 2011 almost 60% (59.9%) of the expenditure of Hungarians (spending per person) covered household costs (25% for housing maintenance and energy and 22.8 % for food) and for the rest 7.5% was spent on culture and leisure, 4.7 % on health, 4% on clothing, 3.4% on tourism and accommodation, and 12.1 % on transport[33].

According to the assessment of the Central Statistical Office[34] in 2010 a Hungarian household with a mortgage loan spent on mortgage payment on average 19% of their total income. However, in case of 12% of the debtors this amount is above 30%, whereas 25% of the debtors were using 20-30% of their full income for mortgage payment.

33 http://www.ksh.hu/docs/hun/xftp/stattukor/haztfogy/haztfogy11.pdf

34 KSH Társadalmi Helyzetkép 2010, Lakáshelyzet, p. 20.

Comparing the expenditure on household costs (60%) with that spent on mortgage payment (19%) reveals that families having mortgage loans can hardly make any savings for other purposes. It should be also added that according to central statistics most families which contracted mortgage loans for housing purposes are families with a higher number of family members than the average and with higher income levels than the average. However, because of higher family members these families belong to the lower income per capita category.[35]

Another recent study published in the Bulletin of the Hungarian National Bank[36] provides information on the factors which have influenced the interest rate expenditures in Hungary. The study emphasises that in Hungary household credit to GDP is relatively low in comparison to other European countries, whereas the related interest-to-GDP ratio is high. It also points out that the ratio of non-performing debtors increased from 1.5 % at the end of 2008 to over 11% and that from 2001 to September 2011 the household credit-to-GDP ratio increased from 10.7 % to 40.6 %. The study concludes that the volume of payable interest is a clear consequence of the growing credit stock. The authors of the study emphasise that international comparison indicates the following:

- As a proportion of GDP the bank credit interest burden of Hungarian households is among the highest in Europe.
- The interest payments of Hungarian households compared to GDP was almost at the same level as in countries with over twice as large household indebtedness as a proportion of GDP as that of Hungary.
- The interest payments-to-GDP ratio in Hungary is also higher in comparison with the Central Eastern European region.
- The ratio of non-housing loans in Hungary is higher within the stock of household loans than in most European countries (excluding Bulgaria and Romania).
- The nominal interest rate on housing loans is the second highest in Hungary behind Bulgaria.
- Hungarian interest rates on non-housing loans are the highest within the entire European Union.

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

No central information is available on this issue. Each bank employs their own conditions. However, according to banking practice, banks do not apply different standard terms depending on the income of the debtor. However, the income of the debtor is taken into consideration when fixing the amount of the loan and the duration of the loan agreement.

   a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate this risk through higher interest rates?)*

No central information is available on this issue. According to banking practice, banks do not employ different interest rates depending on the income of the debtor.

   b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

According to banking practice this is not the case.

   c. *Are there other key terms which change according to the income of the borrower?*

No central information is available on this issue.

35 KSH Társadalmi Helyzetkép 2010, Lakáshelyzet, p. 18-19.

36 G. Szigel and P. Fáykiss: The effect of indebtedness on the financial and income position of Hungarian households, MNB Bulletin, February 2012, 27 ff.

Behaviour of actors in relevant cases

XI. Irresponsible lending practices

1. Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)

Advertising played a central role in the development of the consumer credit market in Hungary. A study published in 2012 [37] mentions among the irresponsible lending practices the aggressive and misleading advertisement and misleading consumer information in the pre-contractual stage. TV advertisements, newspapers and large posters were main instruments of aggressive promotion. Literature criticises the passive attitude of the HFSA towards aggressive publicity, manipulative and misleading practices. The Hungarian Competition Authority several times raised public awareness about such practices especially in its reports to the Hungarian Parliament. Well before the global financial crises and the dominance of the consumer loan market by foreign currency denominated loans, a market study conducted on the market of consumer loan the Hungarian Competition Authority warned the central public authorities (namely the Ministry of Finance, the Financial Supervisory Authority, the Consumer Protection Authority as well as the Ministry for Ministry for Youth, Family, Social Affairs and Equal Chances) that the tools available under competition law to correct the market failures do not suffice to protect the interest of the consumers and urged the adoption of specific rules on consumer credit.[38] However, these warnings did not have an impact on the legislative and credit institutions continued to promote their products under a poor regulatory framework. This is why it is so difficult to find the adequate legal basis outside unfair contract term law to successfully challenge the consumer loan agreements concluded under the liberal legal framework applicable at the time of loan contracting.

The same assessment referred to above, conducted by Pécs University on the market of consumer loan, also emphasised the misleading use of the THM (Total Loan Indicator) by the banks for the comparison of offers. The author highlights that these were suitable for the comparison of fixed interest rate based loans in HUF, but not for loans in foreign currency with flexible interest rates for long run. The banks built their publicity on comparison of the THM of the HUF based loans with those of the loans on foreign currency, which were lower in case of foreign currency. A third practice mentioned in this study is that of loans with delayed reimbursement, when the lower initial reimbursement rates, which did not contain the capital, made the offer attractive for the potential debtor.

Intermediaries also played a significant role in the development of the mortgage market in Hungary, where banking agents promoted loans as a mass product. During the period of the credit boom, 50-60% of the new mortgage loans were marketed by intermediaries. Involvement of intermediaries was a less costly solution for the bank to respond to increasing demand for loans than investing into network development. The legal framework on the activity of the intermediaries (on licensing, training, supervision) was poor. Only after the financial crisis was introduced stricter legislation on eligibility and professional training of banking intermediaries by Law CLIX of 2010 which entered into force in April 2011. Previously, the banks were training their own intermediaries. The intermediaries were not interested in offering to the potential borrowers a product that suits them, because they received their fees depending on the number of contracts concluded.

37 Z. Schepp- M. Pitz, Lakossági devizahitelezés Magyarországon: problémafelmérés és a frankhitelek banki árazásának empirikus vizsgálata, Műhelytanulmány, 2/2012. Pécsi Tudományegyetem, p. 19.

38http://www.gvh.hu/dontesek/agazati_vizsgalatok/2366_hu_jelentes_a_jelzaloghitelezes_targyaban_lefolytatott_agazati_vizsgalatrol.html?query=%C3%A1gazati%20vizsg%C3%A1lat

The large-scale use of intermediaries increased the risks since the banks obtained the information on clients from the intermediaries and not directly from the clients.

After the culmination of the crisis and the decline of the mortgage-loan market many of these intermediaries joined the associations of debtors, or themselves become debtors in payment difficulties.

Finally, distortions of competition in the banking sector developed highly risky products for Hungarian consumers. Before the global financial crisis credit institutions were competing in Hungary by risk competition instead of a price competition, although an interest rate based competition among banks would have contributed to the rise in demand and the formation of a creditworthy client system.

According to a study published in 2008[39] on the basis of the assessments made by the National Bank of Hungary on lending practices, banks had significantly lowered their lending conditions in that period. The study stresses the significant increase registered in the LTV. However, the average value of the LTV was between 50-60% in 2008, for certain mortgage loan categories the banks applied a 100% LTV. As the author of the study concludes, as a result of the soft lending conditions such as the increasing LTV, longer contracts, and low initial reimbursement instalments, consumers with the low financial culture have contracted high risks. Banks have chosen to compete with foreign exchange loans. Risk competition instead interest rate competition further lowered the standards of the loan markets besides the weak regulatory framework on creditworthiness assessment.

2. Was a creditworthiness assessment undertaken before granting the credit?

a. In how many cases were creditworthiness assessments undertaken?

Central information is not available on creditworthiness assessment and such information could not be gathered from banks, since they are reluctant to disclose it.

b. Who was the initiator of the creditworthiness assessment?

The financial institutions were the initiator of the assessment under their own scoring. The scoring is handled by banks as valuable banking knowhow and therefore is not disclosed for purposes of research. Interviews conducted with banks revealed that they do not share their own scoring even with the Hungarian Banking Association.

c. Who undertook the creditworthiness assessment?

According to the exiting banking practice in Hungary even when the loan agreements were concluded through agents, the creditworthiness assessment was undertaken by the bank itself. It differs from bank to bank the internal regulation on who takes the decision on the creditworthiness of the potential customer, a body or a person. Usually, this was not done by the contact persons in the client-bank relation, but by other employees of the bank. There were no legal provisions in place on this matter at the time of the credit boom.

d. What were the criteria of the creditworthiness assessment?

A study published in 2008[40] highlights that at the time of the credit boom there was no behavioural scoring in place in Hungary. Banks employed their own scoring, based on economic and social factors such as: age, domicile, education, income, place of work, family, etc. Before 2011 was missing from the central database on credits a positive list on debtors. Therefore, the banks could not assess the full loan history of the potential borrower.

39 J. Király, M. Nagy, Jelzálogpiacok válságban: Kockázatalapú verseny és tanulságok. Hitelintezeti Szemle, 2008, HETEDIK ÉVFOLYAM, 5. SZÁM, pp. 451-480.

40 *Id*.

e. Was a credit bureau involved?

BISZ Zrt was not involved in creditworthiness assessments in the past.

3. Is there a legal obligation for a mandatory creditworthiness assessment? Is this obligation observed in practice? How are the criteria for creditworthiness assessment in legal provisions?

Creditworthiness assessment became compulsory legal requirement by Government Ordinance No. 361/2009. According to Article 3(1) it is forbidden to grant loans only on the basis of the loan risk ratio. The credit institution must assess the creditworthiness and solvency of the person in every single case. Creditworthiness must rely on the assessment of the incomes of the applicant and on the credit-limit based on income. This law obliges the financial institutions to hand over to the potential debtor the information published on the website of the Hungarian National Bank and HFSA on the risks of indebtedness.[41]

Furthermore, specific loan limits are established by the law for different loan types in Article 4. Accordingly, the monthly reimbursement limit at the moment of approval of the loan request cannot be higher than 80% of the loan limit for EUR based loans. This is 60% for loans denominated in foreign currency. The interdiction does not apply when the debtor has regular income in the currency of the loan and this income is at least equal to all his monthly reimbursement obligations. When establishing the loan limit, the financial institution must take into account all loans the applicant may have with the same or other financial institutions. The credit institution is also obliged to act with due care and make use of all information available in the credit information systems.

For mortgage loans special rules apply, depending on the currency of the loan. For HUF loans the risk exposure cannot exceed 75% of the commercial value of the immovable, whereas in case of financial leasing this is 80%. For loans in euros this is 60% for mortgage loans and 65% for financial leasing. For other currencies a lower limit applies: 45% for mortgage loan and 50% for financial leasing. Financial institutions are allowed to conclude mortgage loan agreements in foreign currency only with persons who have at the moment of the submission of the loan request a monthly net income in the currency of the loan that equals to 15 times the value of the basis income of a full time employee, as established by the National Bank of Hungary (Article 6A.). This restriction does not apply to financial leasing. The rules on loans granted for purchase of automobile establish a risk exposure of 75% of the market value of the automobile and 75% for financial leasing in HUF, 60% in EUR and 65% for financial leasing. For other currencies the rate is 45% for mortgage and 50% for financial leasing. The HSFA is in charge of guarding over proper implementation of these rules. This role was taken over as of October 1, 2013 by the National Bank of Hungary which integrated the HFSA.

4. Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?

This data is not made public by the banks. An interview conducted with the Hungarian Banking Association revealed that banks usually delete the information on refusal to grant the credit. As reason for this was the requirement of equal treatment of customers and that of purpose-oriented recording of data on costumers.

5. Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?

There is no data recorder centrally and banks do not provide data on incidents when the creditor bank or the intermediary failed to explain to the customer the consequences of the default. Since this is included in the written agreement between the parties it could easily be that the banks did not pay specific attention to also provide oral explanations on this matter.

41 The information is available at http://felugyelet.mnb.hu/data/cms2152112/tajek_tulzott_eladosodas.pdf

Before the implementation of Directive 2008/48 the main tool on pre-contractual information was a private law one: the requirement that the contract should be concluded by public notary, who is obliged by the law to read the content to the parties concerned and to explain the legal consequences of the obligations undertaken by the parties under the contract concerned. However, upon the request of the consumer or of both parties this time-consuming procedure was often skipped in practice. Even when it was taken seriously, one may wonder whether a public notary, not being a specialist in banking and finance, was in the position to provide information upon which the consumer would have been in the position to take an informed decision on the risks of the proposed contract. Therefore, this requirement was taken formally in most of the cases, and exhausted by a quick read of the contract. The implementing law of Directive 2008/48 remedied this regulatory gap.

6. Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?

No data and no studies are available in Hungary on this issue.

XII. Irresponsible borrowing practices – emphasis on mortgage

The Working Paper published in 2012 by the University of Pécs mentions as potential behavioural failures of the loan consumers: overconfidence, over-placement, too much optimism on labour market and income level and confirmation bias on loan risks.[42]

1. Did the consumer read the agreement before signing?

According to currently applicable legislation, the consumer must sign a declaration on the loan risk before the conclusion of the loan agreement. However, such formal legal requirements were not in place before and each bank had its own practice on this issue.

2. Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?

The THM (Teljes Hiteldíj Mutató/Total Loan Indicator) upon which the consumer could compare the offers of different banks is in place in Hungary since 1997 (Government Ordinance no. 41 of 1997). Article 8 defined it as being the internal interest rate, which consists of the capital and loan costs payable by the client. These provisions were further detailed by Government Ordinance no. 83 of 2010. Article 200/A. of the Government Ordinance prescribes only from November 27, 2010 that the conversion of HUF both at the time of the availability of the loan for the client and at the time of reimbursement should be either at the exchange average rate established by the bank or at the official exchange rate of the National Bank of Hungary. In addition, Article 209 (1) (g) demands that the financial institutions must mention in the general conditions and terms the calculation method employed and must indicate the moment when the amount established in HUF will be established. The rules in force before 2010 did not required that the exchange rate charge should be separately indicate in the THM.

The legal literature questions whether the use of the THM in advertisements at the time of the credit boom was sufficient guidance for the potential client to compare the offers especially in case of loans denominated in foreign currency It is argued that the THM is fully unsuitable for the comparison of loans denominated in foreign under fluctuating interest rates or for the specific costs of the whole implementation period of the agreement.[43]

42 Z. Schepp- M. Pitz, Lakossági devizahitelezés Magyarországon: problémafelmérés és a frankhitelek banki árazásának empirikus vizsgálata, Műhelytanulányok 2012/1, p. 18

43 Z. Schepp- M. Pitz, op.cit, p. 14.

In its OTP judgement, issued in June 2013, the Kúria confirmed that in case of loans denominated in foreign currency the THM is not suitable for the consumer to calculate his reimbursement costs for the full period of the loan in advance, it cannot provide information on the evolution of the exchange rate between the national currency and foreign currency, because this is independent by the influence of the parties to the contract. It also established that the difference between the purchasing and selling price is a matter of banking policy depending on its business interests and on the demand and offer on the market.

Today, the HFSA has on its website two programs which may guide consumers to compare the financial products of different banks. These are the 'loan and leasing products choice program' with a user manual and the 'loan calculator'. By introducing the data of the financial product offered by a specific bank in the loan calculator, the consumer may obtain information on the estimate development of the instalments to be paid and can be also modelled the effects of interest rate and exchange rate changes. However, the HFSA warns the consumers that the program works with the data provided by the banks and therefore it does not assume liability for the information and data used by the programs.

3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*

This information could not be obtained from the Hungarian Banking Association.

4. *How much time did the consumer take before signing the agreement?*

The procedure of signing a contract is relatively complicated. This lasts up to one month.

5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

According to the Association of Mortgage Banks no instances of withdrawal can be reported.

Litigation

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*

There is no official central data in Hungary on the number of litigations relating to mortgage loans or consumer loan agreements, in general. The reason for this is that courts do not record these cases separately. However, at end of two parallel assessments 2013 were made in Hungary on the actual number of litigations on consumer loan agreements. One was conducted by the Kúria, which asked for data from courts and another by the Hungarian Banking Association that asked for data from banks. The result of both assessments was that there are more than 2000 cases, most of them still pending.

   a. *What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?*

In Hungary one can distinguish between two generations of mortgage loan cases from the point of view of the legal basis of the litigations and a third generation of case law appears to be evolving based upon the impact of the recently issued *Kásler* ruling (C-26/13) of the CJEU.

The first generation of cases were built mostly on the general provisions of the Hungarian Civil Code on contract validity and the regulatory law in place at the time when these contracts were concluded

(before 2008). Cases decided under the UCT Directive were before 2013 far behind these, in number and impact. The second generation of cases evolved at the beginning of 2013, especially when the courts outside Budapest started challenging the loan agreements under the unfair consumer contract terms law. Thus three main categories of legal basis can be identified: i) general contract law (invalidity: for usury, immorality, unethical clauses, etc.), ii) the implementing norms of the UCT Directive (Article 209A Civil Code), and iii) the provisions of regulatory law on the content of credit agreements (the THM/Total Loan Indicator, the exchange rate of reimbursement in case of foreign currency denominated loans, unilateral amendment of the agreement by the credit institution).

The first consumer mortgage cases usually tested the judiciary with a 'basket of legal bases' from the Civil Code, aimed to achieve at any price the nullity of the contract. It is at least surprising why the implementing rules of the UCT Directive (Article 209 A of the Civil Code) were not employed in order to challenge contract fairness. For example, in the *Jörös* case, which was decided by the Pest Central District Court in 2010 and later referred for preliminary ruling to the CJEU (Case C-397/11), the debtor requested the court to establish nullity of the contract on the reason that the clause allowing the bank to unilaterally change the interest rates and other costs of the loan is "usurious, unethical and fictitious in nature". The court dismissed the allegation for lack of sufficient evidence. On appeal at the Budapest Municipal Court the plaintiff changed the legal reasoning and built the case on the argument that the clauses practiced by the bank are "contrary to ethical practice".

The attempt to use general contract law to provide contractual justice between the credit institutions and the consumers has failed if seen from the point of view of the debtors, since most of these cases were won by the credit institutions. The Kúria reacted too late to this reality and only in December 2013 issued a law unification decision (no. 6/2013) in which acknowledged that the standard consumer loan agreements cannot be challenged under the general rules on contract law.

One must also mention in this context that neither rules of the old Civil Code[44] nor the case law contained specific rules on the consequences of invalidly of the contract for reasons of unfairness. There was only a general rule in place, Article 237, which states that the situation before contract conclusion must be restored and in case this cannot be done, the court will declare the contract valid for the period before the adoption of its decision. However, the invalid contract can be declared valid, if the cause of invalidity, especially in case of usury the disproportional disproportionally between the obligations of the parties can be remedied by the exclusion of the disproportional advantage. Article 239 (1) further states that in case of invalidity of certain parts of the contract, the whole contract will be invalid only when the parties would not have concluded the contract without the invalid part. However, it is also open the room for special legislation can render this question differently**.** Besides this general rule, Article 239 (2) contains a special provision for consumer contracts, which states that the whole contract only then will be invalid for reasons of invalidity of some parts of it, if the contract cannot be performed without the invalid part". The Kúria in its law unification decision no. 6/2013 issued in December 2013 reinforced that under Article 239(2) in case of consumer contracts the court must not assess whether the parties would not have concluded the contract without the invalid term, but whether the contract can be enforced without that term.

Only in the last two years are the number of judgments, especially at lower court level, on the rise which try to challenge under the UCT Directive 93/13 the fairness of the agreements concluded in the past under a missing or weak regulatory law, which allowed the credit institutions unlimited freedom in establishing the content of the loan agreements, including the conditions of unilateral contract amendment. On the basis of the few decisions published so far, one can establish that it was not the Kúria but the lower courts who were the actual promoters of the Hungarian developments of unfair contract terms law in the field of consumer credit. However, when such decisions end up at the Kúria, it is more hesitant to assess fairness than the lower courts, and usually opts to ask from the CJEU

44 The new Civil Code entered into force on March 15, 2014.

further guidance. Thus, both the lawyers and the consumers were seeking from the CJEU 'ultimate justice', although the last say remains with the national courts even upon the preliminary ruling of the CJEU.

Before entering into a review and commentary of the highest court cases and of the Hungarian preliminary references to the CJEU, one should also mention another (procedural) particularity of the consumer loan litigations, which causes significant legal uncertainty and hinders effective contractual justice. Article 239A of the Civil Code (introduced in 2012) allows the debtor to ask the court only for a declaratory judgement on contract invalidity without ruling on the legal consequences of the invalidity between the parties. Therefore, in many cases it was left to the parties to settle the consequences of invalidity, either under an out of court settlement, including a deal with the bank, or within a subsequent litigation on the restorations of the situation before contract conclusion. The Hungarian Banking Association expressed its fears about the legal uncertainty such declaratory judgments may later cause, if in the subsequent litigation on the legal consequences of a void contract, the court will re-establish contract validity. The Kúria brought to an end this debate on November 25, 2013 in its law unification decision no.5/2013 in which reinforced the above mentioned practice establishing that in declaratory cases submitted under Article 239/A of the Civil Code *"*the defendant can submit a counter-claim on the legal consequences for the parties, only if does not dispute the contract invalidity, so that admits the claim of the applicant*"*. In its decision the Kúria reassured the evolving practice of some courts which made subject the acceptance of the banks' counter-claim for establishing the legal consequences to previous recognition by the bank of the grounds of invalidity invoked by the debtor. It is worth mentioning that this approach preserved also in the new Civil Code in force since 15 March 2014, in Article 6:108, so that the rules seem not the change in the future. The provision may be qualified nothing less than a genuine social protection measure, for the benefit of consumers in payment difficulty until new rules will be enacted either by the Kúria or by the Government to handle the social and economic consequences of mass over-indebtedness.

b. What were the issues in question? (ie: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)

The vast majority of these litigations concern loans denominated in foreign currency.

The case law assessment study commissioned by the Kúria in 2012 mentions the following issues challenged in court by the debtors of consumer loan agreements[45]:

- Unfairness of the unilateral amendment of the interest rate and costs of the loan agreement under Article 209A of the Civil Code.
- The question whether in case of loans denominated in foreign currency the foreign exchange rate marge is a cost or a calculation method, since under the loan agreement the debtor received HUF and has to reimburse the loan in HUF. The foreign currency was used as a reference basis of the value of the loan. This because the term of costs of the loan was not defined by the law at the moment of contract conclusion.
- Infringement by the creditor of the information obligation provided for in Article 8(3) of the Government Ordinance no. 41/1997 on the THM.
- Nullity of the contract on the reason that the exchange rate marge was not included in the THM, based on Article 231 (1) and (2) of CXII. Of 1996.
- Nullity of the contract because unilateral amendment contravenes Article 7(1) of the Civil Code on the requirement of good faith and honesty.
- Nullity of the contract in case of loans denominated in foreign currency on the basis of Article 207 Civil Code on sham because between the parties did not take place sale –purchase of foreign

45 http://www.lb.hu/sites/default/files/joggyak/joggyakorlat_osszefoglalo_velemeny.pdf

currency. So that the banks charge the client for fictive costs since the risks of the loan are covered by the interest rate. Therefore, the client is charged twice.

- Nullity of the contract for usury, according to Article 202 of the Civil Code.
- Nullity of the contract for infringement of the requirement of good moral, according to Article 200 (2) Civil Code.

c. What were the predominant issues (before and after 2008)?

The issues dominating the judicial debate on consumer credit law in the past 3 years are the best summarized in the law unification decision (Decision no.6/2013) of the Kúria, published in December 2013. The decision enlists those legal questions raised by the case law that plead for clarification:

- Is a foreign currency denominated loan a foreign currency loan or a national currency loan?
- Are these loan agreements void (illegal, against good moral, unfair, usurious, sham, mistake, defective consent)?
- What information obligation had the credit institution at the time of contract conclusion and the legal consequences of missing consumer information?
- What possibilities have the courts to remedy the effects of changes in circumstances occurred subsequent to contract conclusion for one of the contracting parties?
- What are the legal consequences of nullity (the room of the court to declare valid the contract, to restore the initial situation), when and which remedy can be applied by the courts and under which circumstances?
- Does the finding of invalidity affect the whole contract or only part of it, what are the consequences of partial invalidity?
- When do the contract clauses allowing unilateral amendment of the contract by the credit institution comply with the requirement of transparency (only when the consumer itself can establish the proportion of changes caused in interest rates, costs and amendment of the loan by the subsequent changes in circumstances, or it is sufficient the transparency of the list of reasons allowing the unilateral amendment of the contract by the credit institution and is possible to establish that the amendments complied with the requirement of effectiveness, proportionality and symmetry)?

The Kúria came to the conclusion at end of 2013 that the loan agreements denominated in foreign currency are foreign currency loans despite the fact that the customer received the loan and pays the debt in HUF in the hope that its finding brings to end the political debate that the credit institutions provided to the consumers "defective products" in form of foreign currency denominated loans. In the Kúria's view is nothing wrong in that the subsequent risks of the exchange rate fluctuations were fully transferred onto the debtors, because they have contracted the loans under more favourable circumstances than the available loans in national currency at the time of contracting. This is why these loan agreements do not contravene the law since the whole risk is on the debtor and thus they do not infringe the requirements of good morals, are not usurious or sham, and do not aim an impossible obligation for debtors. In line with the above finding, the Kúria considered that the information obligation of the credit institutions does not include the obligation to inform the debtors on the amount of changes in exchange rates. However, the credit institutions must inform their clients about the possibility of exchange rate fluctuations and the effects of such fluctuations on the instalments. The Kúria rejected the possibility for the courts to declare such contract invalid upon the request of the debtors, because the grounds of invalidity must exist at the moment of contract conclusion, which is not the case.

On the question on the consequences of invalidity, the Kúria's instruction towards lower instances is that if the debtors ask in a separate suit the legal consequences of invalidity, the courts "must care above all for contract validity" subject that the causes of invalidity may be excluded or these have

disappeared meantime. When the contract may be kept in force without the invalid parts, the invalid clause will not have legal effects, but the rest of the contract will be binding on the parties.

Besides the concrete rules mentioned above, the law unification decision no. 6/2013 is seminal also because the Kúria makes public also the role it is ready to assume as adjudicator of justice within the crises of consumer loans. Thus, it emphasised that the courts may intervene in individual contracts concluded in the past only exceptionally under Article 241 of the Civil Code[46] and it is impossible to solve in a satisfactory manner within individual litigations the social scale consequences of contracts affecting similarly large groups. Therefore the Kúria argues that judicial action is not the solution for social problems causing high number of cases, considering that judicial problem-solving is time consuming and costly compared to the possibilities of legislative intervention "*as legitim instrument*" for solving social problems. It further suggests that if the legislative makes use of Article 226 (2) of the Civil Code, then besides that it can balance the interests of the parties, it can also take into account the general interest of the society.

Decision no. 6/2013 does not deal within the Hungarian context with the UCT Directive 93/13 for the reason that questions on the unfairness of foreign currency denominated loans referred to the CJEU in 2013(Case C-26/2013) were still waiting at that time for ruling in Luxembourg. These were:

- Is the clause on the exchange rate of the currency in loan agreements denominated in foreign currency part of the main subject matter of the contract? If that is not the case must it be considered that the difference between the buying rate of exchange and the selling rate of exchange constitutes remuneration and it's equivalence with the service provided cannot be analysed from the viewpoint of unfairness? In this regard, does the question whether there has in fact been a foreign exchange operation between the financial entity and the consumer have any impact?
- Must the contractual clause in them appear to be clear and intelligible to the consumer from the grammatical point of view or, in addition, must the economic reasons for using the contractual clause and its relationship with the other contractual clauses also be clear and intelligible?
- Must Article 6(1) of the Directive and paragraph 73 of the judgment of the Court of Justice in Case C-618/10 Banco Español de Crédito be interpreted as meaning that the national court is not entitled to eliminate, for the benefit of the consumer, [the causes] of ineffectiveness of an unfair clause included in the general conditions of a loan contract concluded with a consumer, amending the contractual clause in question and completing the contract, not even where, otherwise, if such a clause is eliminated, the contract cannot be performed on the basis of the remaining contractual clauses? In that regard, is it relevant that national law contains a provision which, in the event of omission of the ineffective clause, governs [in its place] the legal question at issue?"

The *Kásler* case, submitted to the CJEU for preliminary ruling in February 2013 is deeply testing the Hungarian judicial approach on the UCT Directive 93/13. In *Kásler* the applicant achieved at first and second instance on the basis of Article 209A of the Civil Code (the implementing norms of Directive 93/13) to have declared unfair the contract clause on the exchange rate applied for the reimbursement of the loan for the reason that this is unjustified and because it grants unilateral advantage for the creditor. The second instance court however, instead of declaring the unfair clause void, amended on the basis of Article 237 (2) Civil Code the way that the loan must be reimbursed at the buying exchange rate instead of the selling exchange rate**.** This decision was challenged by the creditor bank at the Kúria, which asked guidance from the CJEU.

The Kúria in fact raised the possibility of a solution to transfer the legal and political discourse on consumer credit law from the field of regulatory measures back into contract law, more specifically into the domain of dispositive rules. This is a major turning point in Hungary, if read together with the

46 Article 241 Civil Code: The court may amend long term contracts when circumstances subsequent to contract conclusion substantially affect the interest of one of the contracting parties.

subsequent law unification decision (no. 6/2013) in which the court pleads in favour of legislative intervention into the contract concluded in the past, since as it argues it is not the job of the courts to provide individual justice by adjudicating on the legality and fairness of the specific contracts.

In its reasoning for the preliminary reference in emergency procedure, the Kúria gives voice in very simple terms to the Hungarian reality that providing justice in the field of consumer loan agreements is not simply an issue of individual justice and is no longer a private law problem, but it is viewed primarily in its political, economic and social dimensions[47]. However, the president of the CJEU rejected on April 10, 2014 the request of the Kúria, recalling its earlier case law that neither the risk of economic losses (C-241/09 Fluxys, para. 11.) nor the economic sensitivity of the case (C-201/08 Plantanol, para. 9) justifies the preliminary ruling in emergency procedure according of Article 105 (1) of Treaty.

For the purposes of this Report the preliminary ruling of the CJEU issued in *Kásler* on April 30, 2014 will be assessed above all from the point of view of the tools, criteria and methodology that can be deployed and employed from it by the Hungarian courts when assessing the fairness of the consumer mortgage agreements within the context of the national law.

However, before assessing the ruling from this point of view and making estimates on its future impact on the Hungarian judiciary and policy on consumer over-indebtedness, it is important to stress that the ruling of the CJEU as tool to address the consumer credit injustice was overestimated from the very beginning by all the parties affected by the social, political and economic consequences of consumer over-indebtedness in Hungary. This is why significant space is dedicated to commenting on the *Kásler* ruling within the context of the Hungarian judicial culture and policy, since this judgement may give raise to a third generation of judgements and may create ground for a new approach in the Hungarian policy on handling consumer over-indebtedness. Firstly, the Kúria, after referring its questions to the CJEU in January 2013 had strictly refrained from dealing in subsequent judgements with the UCT Directive 93/13, in general. However, lower courts indeed started testing on a large scale from the beginning of 2013 the potential of the Hungarian implementing rules of the UCT Directive 93/13 to provide individual justice to over-indebted consumers. These lower courts are now seeking reinforcement in the ruling of the CJEU. Hundreds of debtors see the CJEU as an instrument to obtain justice, whereas the credit institutions hope that the ruling of the CJEU may put end to the legislative intervention into contract concluded in the past. Thus, the actual impact of the *Kásler* ruling on effective enforcement of European unfair contract terms law in consumer credit cases and on the future evolution of the balance between *regulatory intervention by the state v. judicial justice provided by courts*, depends to a large extent on the message of the CJEU on the law-framing role of the national courts.

The reaction of the Hungarian mass media to the *Kásler* judgment is perhaps most illustrative of the exaggerated expectations in Hungary towards the preliminary ruling of the CJEU. Strikingly the central message picked up from the ruling of the CJEU, and largely articulated as the key for providing justice to the debtors, is the standard formulation of the preliminary rulings in general, that 'it is for the national courts to establish' contract unfairness upon the criteria proposed by CJEU. This standard statement was perceived as cardinal point of the ruling, because of the judicial policy of the recent years in Hungary, characterised by the hesitations of the courts to apply the unfair contract terms law in the consumer credit litigations, shifting the task to provide justice to the legislature. The hesitations of the Kúria and the focus of the lower courts on general contract law caused significant

47 The grounds advanced in justification of the request for emergency procedure are that "court cases have direct and significant effects on the functioning of the Hungarian banking system and on the whole national economy, which directly affects welfare of a significant percentage of Hungarian population". The Kúria also mentioned in support of its request that according to the official statistics of the National Bank of Hungary from 2012 the debts of the Hungarian households made up 32.56 % of the GDP out of which the foreign currency denominated loan represent 18.54% of the GDP.

loss of trust in civil justice in the field of consumer credit by both the debtors and the politician. Thus, before commenting on the actual ruling of the CJEU it is important to review the judicial messages that can be deduced from the ruling by the Hungarian courts on their role in providing justice in consumer credit litigations.

The most important is certainly the reminder of the CJEU of the policy beyond the UCT Directive 93/13, namely the need to consider the consumer as the weaker party (Paragraphs 39, 72, 74). This hopefully will reinforce the Hungarian courts in viewing the debtors as consumers in need of special protection granted by the unfair contract terms law, for which the traditional principles of contract law, which have been proved to be unsuccessful in handling consumer credit litigations do not suffice. In this regard the CJEU is more firm than AG Wahl was in his Opinion, in which one could not find the typical consumer policy argumentation. Secondly, the criteria proposed by the CJEU in clarifying the legal issues referred to it strengthens the role of the private law courts as adjudicators of justice and the function of individual justice in the field of consumer credit.

The CJEU with few exceptions does not provide substantive criteria, but emphasises the role of judicial assessment, based on the wider legal context and factual circumstances of the contracts (Paragraphs 51, 74). In this direction there is also the weight conferred by the CJEU to pre-contractual information in assessing whether the contract term is plain and intelligible, as a tool in applying the unfairness test (Paragraphs 62, 70, 74). Thus, the impact of the specific answers and criteria elaborated by the CJEU to the Hungarian court should be seen from such a boarder perspective. The judgment of the Kúria rendered on June 3, 2014 in the *Kásler* case based on the ruling of the CJEU seems to confirm this. Firstly, the CJEU established in clear terms that a contract clause that contains a pecuniary obligation for the consumer to pay in instalments the difference between the selling rate of exchange and buying rate of exchange of the foreign currency, cannot be considered remuneration in consideration for a service supplied by the lender that would fall under Article 4(2) of the UCT Directive 93/13. The Kúria imported this finding of the CJEU into its judgement literarily, without any refinement. This will assist the Hungarian debtors to proceed in court in the hope to be reimbursed for the differences between the selling and buying rates of the currency, and will also open the way to unfairness assessment of such clauses on the reason that there are no plain and intelligible.

The CJEU furthermore established that such a term in order to be plain and intelligible should explain the mechanism of exchange in such way that the consumer is in a position to evaluate on the basis of clear and intelligible criteria the economic consequences for him which derive from it. In the view of the CJEU it follows from the requirement of transparency to determine whether the contract established transparently the reason for and the particularities of the mechanism for converting the foreign currency and the relationship between that mechanism and mechanism laid down by other terms relating to the advance of the loan, so that the consumer can foresee the economic consequences for him deriving from it. Are relevant all information such as advertisement, promotion in the negotiation of the agreement on the basis of which he would not only be aware of the existence of the difference, generally observed on the securities market, between the selling rate and the buying rate of the exchange of a foreign currency, but also to assess the potentially significant economic consequences from the application of the selling rate for the calculation of the repayments and therefore the total sum of the loan. This reasoning of the CJEU will be of major assistance for the Hungarian judiciary.

By the method of assessment it proposes for establishing intelligibleness and plainness of contract terms the CJEU brings under the umbrella of the unfairness test issues that due to the weak and overly permissive legal framework on consumer credit at the moment of contract conclusion, could not be subsequently handled under the general contract law, such as the issue of information-obligation and the advertising practices. It also serves as solution for a serious legal gap that in the past blocked the possibility of challenging the loan agreements on the ground of missing or misleading pre-contractual information. Indeed, neither the Civil Code in place at contract conclusion nor the regulatory law on the functioning of the credit institutions sanctioned the infringement of the information obligation, the

provision of false information or non-provision of information with the nullity of the loan agreement. As a result, contracts and clauses concluded under the infringement of the information obligation were considered by the decision no. 6/2013 of the Kúria as not contrary to law in lack of any legal sanctions provided by the law. The *Kásle*r ruling gives the green light to the very cautiously proposed solution of the Kúria, advanced in December 2013, to remedy this legal gap under the rules on misleading consent and error at the moment of contract conclusion, which may cause unfairness of the contract. The Kúria considered important to stress in December 2013, that such line of remedy will depend on the opinion to be delivered by the CJEU in the *Kásler* case. However, the most hotly anticipated answer from the CJEU that will definitely have the highest impact on subsequent developments in the Hungarian case law is that allowing the courts to substitute the unfair term with a provision of the national law in case the contract could not be kept in force without the unfair terms (Paragraphs 81-82).

This solution on one hand relieves the courts from the burden of adjudicating on individual basis on what would have been the correct clause under the given circumstances in case of more than 2000 litigations and on ruling on the consequences of contract nullity for the contracting parties that was shifted in 2012 to alternative dispute settlement. The solution definitely brings more legal certainty into the market. On the other hand, seen within the Hungarian legal landscape this solution will not bring to end the legal and judicial discourse on contract freedom and regulatory intervention into the contracts concluded in the past. This because the CJEU answered the question referred to it in more general terms than the initial question of the Kúria, which asked whether the court may make use of a dispositive (permissive) rule of the national law. However, the Hungarian translation of the ruling of the CJEU stays bound to the concept of dispositive rule and did the same the Kúria in its *Kásler* judgment issued on 3 June 2014.

The Kúria substituted the unfair term with the provision of the Civil Code in force at contract conclusion- Article 213 (2) that establishes as applicable exchange rate for foreign currency loans the exchange rate at the time and place of performance of loan reimbursement. In addition the Kúria specified that this should be the official exchange rate of the National Bank of Hungary.

By this the private law focus is shifted in Hungary again back to the field of general contract law, since this narrow interpretation limiting at the general, dispositive rules of the Civil Code the freedom of the courts to substitute the unfair terms left outside the field of application of this judicial solution the special mandatory rules in the field of consumer credit law. The Kúria in its preliminary reference searched for a solution from the private law in force at the time of the conclusion of the contract and found a provision on the specific issue (the exchange rate) that for both parties is affordable. However, it did not consider the larger policy and private law implications of the solution for other types of clauses in consumer credit agreements.

Thus, the *Kásler* ruling of the CJEU will not bring to end the wave of Hungarian references for preliminary ruling, but it will give rise to post-*Kásler* references since its perception by the highest court is not in full compliance with that of the CJEU. This policy of the Kúria may create ground for conflicting case law, since some lower courts may stay bound to the broad interpretation of the CJEU, whereas others will be guided by the Hungarian translation and the Kúria's own interpretation on the *Kásler* ruling, although the *Kásler* judgment of the Kúria does not have binding force on the courts. The Kúria did what the CJEU does so often: reframed the answer of the CJEU according to its policy aims. However, the immediate policy impact of the *Kásler* ruling is indisputable. Shortly after its *Kásler* judgment the Kúria adopted a law unification decision (No. 2/2014) on 16 June 2014 on further major questions seeking judicial answer in Hungary:

- Is a contract concerning a loan denominated in foreign currency unfair based on the reason that the whole exchange risk was transferred against a favourable interest rate onto the consumer?
- May cause on reason of lacking transparency the provision of contradictory, poor, or false information to the consumer the unfairness of the clause on exchange rate risk?

- Upon which criteria can be established the transparency of the clauses on unilateral amendment of the loan agreement?
- Can the clauses on the application of different exchange rates for transfer of the loan and reimbursement of the loan be considered unfair and what will be the consequences?

Firstly, The Kúria considered that unfairness of a clause allowing unilateral amendment of the loan agreement by the credit institute should be established on the basis of its own judicial criteria, developed in its former opinion (no. 2/2012 (XII. 10) PK point 6): plain and intelligible wording, effective determination, the requirement of objectiveness, the principle of effectiveness and proportionality, the principle of transparency, the principle of symmetry and the right to contract termination. The clause will be not unfair when on the basis of the above principles it was plain and intelligible for the consumer the way and manner in which the clause on unilateral amendment of the contract by the credit institute may affect his payment obligations.

Then on the issue of unfairness of clauses transferring the whole exchange risk onto the debtor in exchange of a favourable interest rate, the Kúria established that as main rule such a clause belongs to the main subject matter of the loan agreement and therefore does not fall under the unfairness test, except that for the generally informed, reasonably circumspect and cautious average consumer the clause was not plain and intelligible, taking into account the wording of the agreement and the information received from the credit institute. If on the basis of the inadequate information received or in lack of information the consumer had reasons to believe that the exchange risk is not real or it will be affected by such risk only in a limited manner, the clause rendering the exchange rate risk is void, causing the partial nullity or full invalidity of the loan agreement.

Furthermore, the Kúria considered per se unfair the clauses establishing different exchange rates for the transfer of the loan and reimbursement of the instalments in case of loans denominated in foreign currency on the reason that the consumer does not receive any service in exchange of this risk, causing for him unreasonable costs. In the view of the Kúria, such clause is unfair also for the reason that it is not clear and intelligible and transparent for the consumers the economic justification of the different exchange rates applied by the credit institution. However, on the consequences of finding such clauses unfair, the Kúria went further than what it has established in its *Kásler* judgment (the judicial replacement of the unfair clause with a dispositive provision of the Civil Code in force at contract conclusion) and considered it only as a temporary way out until mandatory rules will be adopted by the legislative.

Both the *Kásler* judgment and the law unification decision reveal the high policy impact of the *Kásler* ruling of the CJEU, although it is too early to make estimates on its private law impact. It will certainly encourage large number of debtors to seek justice in civil law courts under the Hungarian implementing rules of the UCT Directive 93/13. The major change in the judicial policy of the Kúria is the consumer policy reasoning that is explicitly formulated in the law unification decision. On one hand the consumer is considered an active market player (reasonable informed, circumspect and cautious), whereas on the other hand the Kúria acknowledges only after a few weeks upon its *Kásler* judgment that the use of the general rules of the Civil Code on exchange rate in case of loans denominated in foreign currency may not be a suitable solution, inviting the legislative to issue mandatory special rules. However, despite of this promising turn in the highest level judicial policy which put hopefully end to the judicial reluctance of the recent years, the *Kásler* ruling of the CJEU and the recent judgments of the Kúria will not bring soon to an end the consumer loan litigations in Hungary, nor the wave of the Hungarian preliminary references to the CJEU. Although, it is a major achievement in Hungary that the Kúria brought the policy discourse back to the field of contract law from that of regulatory intervention into private contracts in search for solution on ex post contractual justice in agreements concluded in the past, at the end the Kúria again shifts the game back to the legislature, when it is about rendering justice on the consequences of unfairness for the contracting parties.

This, in the opinion of the Kúria, as results from its first official declarations on the consequences of the law unification decision issued on June 16th, 2014, will be the task of the legislature. Thus, the question of restoration of the situation before contract conclusion in case of finding contract invalidity for reasons of unfairness and that on how will be the consumers compensated in case of partial contract invalidity are again perceived by the Kúria as matters exceeding the domains of individual justice. In fact the courts do not have yet the tools to render contractual justice soon for thousands of consumers. In addition, in applying the unfairness control the courts still may face series of difficulties arising out from the domestic civil procedural law on which new references for preliminary ruling will certainly reach the CJEU. This new generation of references started arriving to the CJEU since the beginning of 2013 starting with Case C-567/13 *Baczó és Vizsnyiczai* and Case C- 32/14 *Erste Bank.*

Thus, the Hungarian courts will continue to be promoters of further judicial development of the European law on unfair contract terms law. This does not mean that in other Member States do not develop similar interpretation problems of the UCT Directive in the context of the domestic private law and civil procedural law. However, the difference is that in Hungary such interpretative problems are usually exported to the EU level, instead of being solved by way of judicial development of the domestic law. The questions referred by Hungary to the CJEU on the interpretation of the UCT Directive well illustrate how the transfer to the European level of legal issues that the domestic judiciary and legislative is not able to solve enhances the CJEU in assuming more and more law framing role in judicial unification of contract law, with consequences onto all the Member States.

However, from the law unification decision No. 2/2014 issued on 16 June 2014 it does not result that the Hungarian Kúria had fully assumed such a role. It seems from its approach that in Hungary justice rendering in the field of consumer credit continue to be a shared competence between the Government and the judiciary. The *Kásler* ruling of the CJEU did not have impact on this policy approach of the highest instance of the Hungarian judiciary.

2. *Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?*

Class actions are not known in consumer law litigations. In almost all of the very few cases closed so far the initiator of the litigation is the individual consumer and rarely the public prosecutor (litigations in public interest). The plaintiff is the debtor in payment difficulty who tries to obtain nullity of the contract. There is no data available on the percentage of cases where interest groups of consumer debtors initiated litigations.

3. *What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?*

There is no centralised data available at the National Office of Judges on the number of consumer loan litigations or mortgage loan litigations, including details such as those in the question above. The case registries of the courts do not keep records of civil law cases on the basis of the legal basis or of the legal issues concerned, such as unfair contract clause, consumer loan, etc. Court records use the heading "contract invalidity" for all types of cases.

4. *Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?*

Class action is not known in the Hungarian law. However, consumers can be represented in litigations by a collective entity, which represent the interest of those affected and by state authorities.

The use of *actio popularis* in consumer credit cases is possible under Hungarian law, although this is not straightforward. The prosecutor is authorised under the Act of Civil Procedure to act when the person is not able to defend themselves. This authorisation is broadly interpreted in Hungary. In

addition to this general legal base, the Consumer Protection Act (Law no. CLV of 1997 as amended by Law LV of 2012) provides for two additional possibilities to defend public interest in consumer matters. Article 38 stipulates the right of the consumer protection authority and of consumer protection associations to submit civil law suits in cases when consumer law infringements established by the consumer protection authority affect large number of consumers. Article 39 establishes the right to injunction of the prosecutor or of the association representing the interest of consumers when significant number of consumers are affected or substantial damage may be caused to them. These entities may ask the court to stop the law infringement and to forbid the practice for the future and to order the restoration of the situation before the infringement. However, the individual consumers are not prevented in such case to submit civil law suits.

Furthermore, Article 209 (5) of the Civil Code contains special rules on the litigation rights of entities in the public interest in cases concerning unfair contract terms. These are: the prosecutor, ministers, head of central authority, professional chamber, associations, and consumer protection authorities.

a. How are those interests defined?

b. What are the requirements for such representation?

Under Hungarian law collective entities seeking to be considered a qualified entity must fulfil the following criterion: they must be established as collective entity under a legal form established by the law, consumer protection must be one of its declared scope of activity, must have been active for at least two years and must have at least 50 members.

5. In practice, is litigation in "public / diffuse interest" more common than individual litigation?

There are too few court decisions so far to reveal conclusive findings. Most of these decisions were adopted in cases initiated by individual consumers. From the very few cases finalised so far it can be concluded that most of the cases are submitted by the individual consumer. From the case law assessment of the Kúria undertaken in 2012 results that out of 26 judgements nineteen were initiated in public interest, seventeen by prosecutor, one by the HFSA and one by the consumer protection authority.

6. Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?

The dispute settlement body for financial disputes, the Financial Arbitration Board (FAB), was established under Law no. CLVIII. of 2010 and started its activities on 1 July 1 2011. This body functioned within the HFSA, which from October 1, 2013 was integrated into the National Bank of Hungary. The supervisory procedures of the HFSA and of the FAB are complementary.

The out of court dispute settlement procedure can be initiated by consumers in search for a civil law remedy in disputes concerning the conclusion and implementation of contracts on financial services concluded between financial institutions and consumers, including payments, deposits, credit & loans, mortgages, life/non-life insurance, investments, securities, and most pensions. The FAB establishes the infringement and tries to render the dispute under an agreement to be reached by the parties. In the case of unsuccessful settlement by agreement, the FAB will issue a decision rendering the dispute between the parties. The procedure is available only when the consumer has previously tried to settle the dispute with the financial institution. The law imposes on the financial institution the obligation to cooperate with the FAB during the procedure, namely to hand over the documents the FAB may request and to take part in the hearing. In 2012 the FAB had to impose in eight cases fines on financial institutions for infringement of the cooperation obligation.

7. Do consumers make use of out-of-court settlement procedures?

The number of disputes settled by FAB is far higher than the number of court decisions. However, the number of pending cases currently at lower courts shows a tendency of more focus of the consumers on litigation than out of court settlement. The reason beyond this recent development may be the preliminary references sent by the Kúria and the lower courts to the CJEU starting from the beginning of 2013.

If yes:

a. Which ones?

Hungarian consumers prefer the FAB. There is no central information about the use of other out of court settlement bodies. However, from the case law of lower courts we can see that arbitration clauses were currently employed by banks in credit agreements with consumers. Thus a rise in cases to be settled by arbitration in the future is to be expected. However, in a few cases the consumers challenged the fairness of such clauses in court. There are two Hungarian preliminary references at the CJEU on issues concerning arbitration clauses.

b. What is their success rate?

During the first year of activity (2012), complaints handled by the FAB against the banks concerning loan agreements concluded with consumers amounts amounted to 76% of the total number of complaints. The same percentage applies for 2013, when the FAB ruled in 2274 cases. In 48% of these cases the parties reached an agreement with the assistance of the FAB.

c. What are the issues?

FAB dispute settlement is mostly used to render the conflict between the parties in search of ways to avoid the termination of the agreement and less for the clarification of specific legal questions. The parties often reach agreement on the rescheduling of the debt by extension of reimbursement period and establishment of different instalments than those in the initial contract, sometimes even on discharge of certain amounts from the initial loan. There are also cases when the credit institution only makes a commitment towards the client that within a short period of time (usually fifteen days) it will elaborate a plan on debt rescheduling.

There are also cases when the debtors asked the FAB to assist them in making use of rights granted to them by law within the framework of the consumer rescue schemes, upon their direct negotiation with the credit institution has failed. Typical examples are the cases when the credit institution did not offer the mortgaged immovable property for purchase by the state, although the debtor requested this and was eligible for this scheme.

Others have tried to obtain through FAB dispute settlement reimbursement of the amounts they paid to the credit institution as difference between the exchange rate applied at the time of transfer of the loan by the bank (selling exchange rate) and that established for the reimbursement of the loan (the purchasing exchange rate).

Last but not least there are also cases when the parties to a loan agreement denominated in foreign currency reach an agreement to convert the loan into HUF or on final payment.

d. Are there special bankruptcy courts? What is their role?

There is no private bankruptcy law in place in Hungary.

XIV. Impact of the crisis on litigations

1. Has there been an increase in litigation since the financial crisis?

The financial crisis did not have immediate impact on litigation, although shortly after 2008 the payment difficulties of the consumers became manifest. Mostly after 2011 consumers started to

challenge in court the validity of the loan agreements concluded before the crisis. According to the mass media, which picked up the statistics circulated by the banks, in November 2013 there were 2,500 cases in Hungary, out of which a decision was issues in 60 cases. Out of these 60 litigations only in six instances did the bank loose.

However, the courts are not allowed to provide information to the public on on-going cases and no research approval can be obtained on cases which were not yet concluded. In addition, another difficulty in assessing the exact number of on-going litigations is due to the fact that court statistics do not operate with specific concepts such as consumer loan, mortgage loan, or unfair contract terms. The law suits are classified according to the legal basis on which are built and in the majority of the cases the applicant invokes a full set of reasons under general contract law in order to obtain nullity of the contract under the general rules of the Civil Code.

a. How many mortgage agreements where challenged in out-of-court or judicial proceedings before and after the crisis?

No centralised data is available on judicial settlement of mortgage agreements or on how many cases the litigation was settled upon agreement between the client and the financial institution. Banks are reluctant to provide data on their on-going litigations, not disclosing information on the success rate versus failure rate of such cases.

b. What are the issues challenged? In which legal field?

The case law assessment study of the Kúria, published in 2012, identified the following subject matter of the consumer credit litigations:

- Infringement of the obligations of the credit institutions to include all costs in the THM (Total Loan Indicator), in thirteen cases.
- Infringement of good faith or good morals [Article 200 (2) Civil Code], in four cases
- Unreasonable imbalance in the obligations of the parties [Article 201(2) Civil Code], in three cases
- Usury [Article 202 Civil Code] in three cases
- Mistake [Article 210 Civil Code] in one case.

Typical legal issues in judgements published after 2012:

- The legal consequences of the infringement of the pre-contractual information duty by the bank
- Nullity of the loan agreement for reasons of infringement of good morals, usury, sham, mistake, defective consent, unfairness.
- The material field of applicability of the unfairness test (to clauses establishing the exchange rate of reimbursement, unilateral amendment of the contract by the bank)/
- The legal consequences of contract invalidity.
- The right and room of courts to re-establish the contractual balance due to significant change in circumstances after contract conclusion (rebus sic stantibus).
- The right of the court to replace the unfair term

2. Did the Aziz ruling have an impact on national legislation / legal framework?

a. Are there cases before national courts dealing with issues that also arose in the Aziz case?

Although there are many cases that raise the same issues as the *Aziz* case, so far only one final judgement can reported where the court referred to the *Aziz* judgment. That case was rendered on 10 December 2013 by the Appeal Court of Budapest. Interestingly, this decision that can be considered landmark in many aspects did not pick up the central issues from the *Aziz* case but referred to it in

general terms only. However, a recent decision of the same court, issued in February 2014, contains a lengthy reasoning referring to the rules established by the CJEU in *Aziz* [48].

b. What was / is considered an unfair contract term in the national court rulings before and after Aziz?

The study on the analysis of the case law on consumer contracts in the field of financial services, commissioned by the Kúria in 2012, identified totally 26 lower cases where the applicant challenged the fairness of general contract terms and conditions on the basis of 209A of the Civil Code and Government Ordinance 18/1999, the implementing laws of the UCT Directive 93/13. Only in one of these cases did the court analyse contract fairness on its own motion, whereas in the rest of cases this was asked by the applicant. In nineteen cases the litigation was initiated in the public interest: seventeen by prosecutors, one by the HFSA and one by the National Consumer Protection Authority. Unfortunately, the study commissioned by the Kúria does not provide data on the date of these court decisions or on the details of the decisions that would allow an impact assessment of the *Aziz* decision of the CJEU on subsequent Hungarian case law. Hopefully, the reluctance of the Hungarian courts will change with the *Banif* ruling (Case C-472/11) issued in 2013, where the CJEU recalled the obligation of the national court to assess contract fairness on its own motion. The following clauses were challenged:

- Entitlement of the contracting party (the financial institution) to unilaterally interpret contract clauses (three cases)
- Obligation of the consumer to fulfil its contractual obligations even when the other party does not perform their obligations (two cases)
- Exclusion or limitation of the consumer's right to terminate the contract (one case)
- Qualification of the consumer's attitude as contractual will or omission when the time for the consumer to react is too short (one case)
- Unilateral modification of the contract by the financial institution without justified reason settled in the contract, especially the increase of the costs of the contract, or unilateral modification of the contract for reasons mentioned in the contract when the consumer does not have the right to withdraw from the contract or to terminate the contract with immediate effect (fifteen cases).

Out of the 26 judgements, in fourteen cases the court of first instance declared the clause unfair, whereas in twelve cases rejected the arguments of the applicant. On appeal, in sixteen cases the court found the clauses unfair, in nine cases rejected the appeal and in one case referred the case back to court of first instance. As the Study emphasises, only in one case did the court establish unfairness on its own motion, although in many instances other courts invoked on their own motion the exemptions from the Section 209 A, established in Paragraph 5 and 6. These provisions exempt those clauses from unfairness assessment which comply with legal provisions. The confusion of the courts is also generated by the fact that banks invoke as legal basis for the unilateral modification of the contract their compliance with the Code of Conduct that enlists the events when the credit institutions may change the contract. There is no agreement even in the literature whether a clause which complies with the Code of Conduct can be subsequently assessed under fairness considerations. Although the Code of Conduct is enforced by the HFSA, it remains soft law. Thus, such a clause should normally fall under Article 209 A of the Civil Code, i.e. the implementing norm of UCT Directive 93/13. Finally, the Kúria declared at end of December 2012 in its civil chamber opinion no. 2/2012 that the Code of Conduct is not law, therefore the courts may assess the unfairness of clauses complying with its requirements.

From the analysis of the few decisions published by lower courts it can clearly be seen that the courts of Budapest and the rest of the courts outside Budapest had different approaches in the past to

48 Fővárosi Ítélőtábla, 5 Pf.21.122/2013/10

unfairness in consumer loan agreements. Whereas the courts outside Budapest are more committed to assessing such contracts under the unfairness test, the courts of Budapest were more reluctant in the past to proceed under the UCT Directive 93/13. Thus, the Court of Appeal of Szeged in a decision issued last year Pf.I.20.052/2012/7 established that in case of loan agreements denominated in foreign currency the bank does not supply to the consumer sale purchase service for the procurement of the foreign currency, but only binds the instalment to be paid by the debtor in HUF to the exchange rate of the foreign currency in order to maintain the value of the loan granted in HUF. Therefore, a contract clause is unfair which due to the different exchange rate applied by the bank at the moment of payment of the loan and at the payment of the monthly instalments, makes it possible for the bank to obtain an exchange rate margin outside the THM on the basis of the sale purchase prices of the foreign currency. Since a sale purchase of foreign currency does not take place between the bank and the creditor, the bank cannot charge the client for this. In line with this argument the Szeged court established that since the exchange rate difference is not a cost for a service provided by the bank, it does not fall under the exception granted by Article 209 (5) of the Civil Code. Therefore, the clause has been ruled unfair because the bank does not calculate the same exchange rate at the moment of transfer of the loan and that of the reimbursement.

However, the policy of the Budapest courts will also change in the future under the influence of the recent decisions of the Appeal Court of Budapest[49], built on the UCT Directive the case law of the CJEU. One can report in Hungary a significant improvement starting with end of 2013 at appeal court level concerning the enforcement of the UCT Directive in line with the CJEU case law, although one cannot say yet that there is evolving a uniform case law in Hungary.

c. Did Aziz have any other impact on national legislation / legal framework (i.e. in the field of procedural law)? What are those impacts?

Procedural law was not amended in Hungary under the influence of the UCT Directive 93/13 or the subsequent case law of the CJEU. However, the questions referred onto the CJEU by the Hungarian highest court, the Kúria, testify that the Hungarian judiciary hesitates in making use of the rights it has under the EU law to act on its own motion in cases concerning consumer contracts, including consumer loans. The courts seem to fear that their decisions will be overruled by a higher court if compliance with the case law of the CJEU infringes mandatory provisions of the national civil procedural law or the general principles of the domestic contract law. However, the Kúria tries to guide the lower courts via soft law instruments, such as the chamber opinions, in line with the case law of the CJEU. These have, according to a recent study (not yet published) conducted last year on the impact of these opinions, a higher effect on the courts than the law unification decisions of the Kúria. In fact, even the CJEU took into consideration the Kúria's chamber opinion in assessing and establishing that the Hungarian legislation is in line with the requirements arising out from the UCT Directive 93/13 in the preliminary ruling issued in *Jörös* (C-397/11).

3. Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework? Elaborate.

As explained above, the case law of the CJEU had very marginal impact on the first generation cases on consumer credit. The fact that most of these cases were decided on the basis of general contract law and not the UCT Directive is noteworthy on its own regarding about the impact of the European case law in Hungary. In those very few instances did the courts refer to the CJEU case law, case C- 618/10 *Banco Español de Credito* and case C-76/10 *Pohotovost' s. r. o. kontra Iveta Korčkovská* in search for solutions on questions raised by the Hungarian realities in the field of consumer credit law. On the other hand, it is strange that in the past the courts did not make use of the rulings rendered in preliminary references by Hungarian courts to the CJEU on the interpretation of the UCT Directive,

49 Fővárosi Ítélőtábla 5. Pf.21.882/2013/4, decision issued on March 6, 2014 (Invitel, Jörös), Fővárosi Ítélőtábla 5. PF.21.122/2013/10, decision issued on February 7, 2014 (Jörös, Banco Espaniol, Aziz),

such as the ruling in C-243/08 *Pannon* or C- 472/10 *Invitel*, although the Kúria has guided in its civil chamber opinions[50] the lower courts about the developments in the case law of the CJEU.

However, the second generation cases started discovering the potential of Case C-618/10 *Banco Español* (this being the most cited ruling of the CJEU[51]) in providing individual justice in consumer credit cases. Thus, one can conclude that the impact of the case law of the CJEU is rising in Hungary, starting with the end of 2013[52].

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

Consumer credit law underwent significant changes after the financial crisis due to a sharp turn in policy. Hungary switched after 2010 from a liberal policy to a strongly paternalistic regulatory policy.

2. *Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?*

Mortgage law was not affected by the crisis; no significant legislative amendments took place during this period. Court judgements mostly concern the loan agreements and not the mortgage itself. Private bankruptcy law is still in stage of development. The law on unfair contract terms was not amended as a consequence of the consumer credit crisis, and until the year 2013 unfair contract terms law was not largely used as an effective tool for providing justice to the consumers.

Consumer over-indebtedness in Hungary was facilitated by a missing or weak regulatory framework (missing public law measures on financial institutions and on consumer credit), weak implementation of existing laws by public institutions (such as the consumer protection authority, before 2010) and weak judicial enforcement of unfair consumer contract law (hesitation of the courts to invoke the UCT Directive 93/13 on own motion). Therefore, strict rules were introduced after 2010 on financial supervision and consumer credit. In addition, several debtor rescue measures were implemented to cure the social and economic effects of the crisis. These measures deeply redefined the traditional borders of public law and private law in the field of financial services. The new regulatory measures have high deterrent effects on banks and promote ‘distributive justice’ in the field of private banking by debtor rescue measures, the cost of which are shared by the banks concerned and the state budget (the society). However, little is known today about the effects of the public policy measures on debtor behaviour, i.e. to what extent these continuously evolving rescue schemes had worsened or improved the loan reimbursement practice of the debtors. It would have been more effective for the market, including all stakeholders, to have such rescue measures at ones as a never returning opportunity, instead of a ‘process’ based on piecemeal approach.

The major finding on the quality of the new regulation is a delay in legislative responses, which is not the omission of the current government but of the legislative and executive power in place during the credit boom. Therefore, most of the legislative efforts adopted since 2010 are responses to the regulatory failures of the past in the light of present social, political and economic impacts of these

50 For example: 2/2011. (XII.12) PK vélemény (referred to C-240/98 Oceano, C-243/08 Pannon), 3/2011. (XII.12) PK vélemény (referred to C-200/98 Pannon, C-240/98 Oceano), 2/2012 (XII.10) PK vélemény (referred to C-472/10 Invitel).

51 For example: Fővárosi Törvényszék PKfv. 634.687/2013/3 (13.12.2013), Pécsi Ítélőtábla Pf/VI.20.238/2013/9.

52 Fővárosi Ítélőtábla 5. Pf.21.882/2013/4, decision issued on March 6, 2014 (Invitel, Jörös), Fővárosi Ítélőtábla 5. PF.21.122/2013/10, decision issued on February 7, 2014 (Jö

past failures, whereas little energy and room remains for the new regulatory needs of the market that has changed in the meantime. The approach could be labelled as 'post-ante' management of the crisis, since the present regulatory responses bear the burden of the past that implies high risks of regulatory mismatches in spite of the sustained efforts of the Government to come up with effective responses onto the dysfunctions of the 'regulatory market'. However, except the consumer rescue measures, the new rules on the supervision of the credit institutions and on consumer credit contracting apply to newly concluded agreements and thus do not provide solutions for the regulatory failures of the past. Therefore, it seems (and it is perceived as such by the majority of debtors and to certain extent by the Government as well), that the private law impact of the regulatory failures of the past are left to be dealt with by the judiciary (private law courts), the role of the private law vehicles (the contracts) being overestimated among the factors generating the consumer credit crisis in Hungary.

The problems that do manifest themselves within the process of judicial enforcement of the consumer credit contracts (private law contracts) are in fact the result of regulatory failures. However, contract law, including judge-made law, cannot be the substitute for function of regulatory law, due to the fact that the two fields pursue different types of legal justice. Therefore, the Hungarian courts were reluctant for good reasons to use the law-framing role they could have under the EU unfair contract terms law to remedy regulatory failures in consumer credit law. This finding does not exculpate the Hungarian judiciary from its failure to effectively apply the unfair contract terms law in other fields than consumer credit law.

Private law cannot remedy regulatory failures, cannot provide collective justice and is not meant to function as tool of wealth-redistribution as compensation for individual contractual injustice, even when this is caused by standard agreements. This is why, besides the debtors, the judiciary should also be considered victim of the regulatory failures of the past. Thus, its approach that private justice is not the suitable tool to provide effective protection to large-scale consumer over-indebtedness is to large extent justified. However, the judiciary is indeed in the position to restore (as the Kúria attempts) the borders between private law and public law, distorted in the past by the missing regulatory framework and over-distorted by the subsequent regulatory responses that intervened into the private contracts between the credit institutions and the consumers. This attempt of the Kúria, obvious from the solution advanced in the preliminary reference sent to the CJEU in the *Kásler* case, is an important turning point from its previous attitude when it was looking for shifting or at least sharing responsibility with other central public institutions in Hungary and with the EU (by referring questions to the CJEU).

Faced with such realities the Hungarian Government continues to search for new tools to balance the 'missing judicial effectiveness' in the field of consumer credit law. On November 28, 2013 the Government made a request for 'constitutional control of the contract clauses on unilateral amendment of the credit agreements' also challenging the constitutionality of the legal provisions which served in the past as legal basis of such unilateral amendments of the loan agreements by banks and last but not least 'the constitutionality of civil court decisions reinforcing the clauses on unilateral contract amendments by banks'.

The request for constitutional review also advances legal arguments justifying the state interventions which took place since 2010 into private contracts. The arguments submitted by the Government makes reference to Article 226 (2) of the Civil Code that allows in exceptional cases "to establish the content of contracts concluded in the past" especially in case of long term contracts where such subsequent economic and social changes known in advance would have driven the parties to conclude the contract with a different content or not to conclude the contract. It is further emphasised that in case such changes gain social dimension (affects high number of contracts) the change in circumstances may plead for state intervention that should be done under the conditions set up in Article 241 of the Civil Code on judicial intervention under the principle of *rebus sic stantibus*.

Finally it must be mentioned that in this request for constitutional review of the consumer credit contracting, at least the Government questions whether the contracting practice of consumer credit

qualifies as abuse of dominant position in the banking sector. Firstly, it raises the question whether Article M (2) of the Constitution on the obligation of Hungary to guard over free competition, including measures in cases of abuse of dominant position, may be invoked in cases when large consumer groups are negatively affected by specific types of contracts. Secondly, it emphasises that the provisions of the consumer credit agreements on unilateral increase on interest rates and those on exchange rate marge raise the possibility of abuse of dominant position by the concerned banks. It is still a mystery in Hungary, at least for the author of this Report, why those banks which did not practice the "new products" which now are challenged from the point of view of their fairness, did not react by making use of the tools of competition law.

In its decision no. 1769/2013 issued on March 17, 2014 the Hungarian Constitutional Court established that Articles B) 1 of the Constitution on the requirement of legal certainty and M (2) on the obligation of the state to guard over free competition provide legal basis for 'exceptional intervention by law into contracts concluded before it's entering into force, on the basis of the principle *rebus sic stantibus*'. The state may change by law the content of contracts on reasons of constitutionality under the same conditions as required in case of judicial intervention under the private law. However, it rejected the possibility of constitutional review of court decisions on the basis of Article M) 2, although in general the Constitutional Court can review individual decisions. Last but not least, the Constitutional Court established that from Article M) 2 results the obligation of the state to issue the necessary laws for the protection of the interest of the consumers and to assure the functioning of the necessary institutions that repress abuses of dominant position.

The overall impact of the legislative measures taken by the Government in Hungary and the subsequent judicial responses can be defined from a regulatory point of view as clear strengthening of state intervention into the market. The case of Hungary is a costly experience for all affected parties (banks, consumers and the society) on how a poor regulatory and institutional framework that generated weak administrative enforcement can shake the whole legal system (including the private law and the private law judiciary). Therefore, any value judgement on subsequent state intervention into the domain of private contracts should be made from this perspective.

3. What are the changes in particular? Focus on consumer credit and mortgage law.

The focus of the Government is on consumer credit law and less on mortgage law, which remained mostly unaffected by the policy measures adopted after 2010, except the eviction quota, state purchase of the mortgaged immovable and other measures on eviction moratorium (for example the winter moratorium). Consumer credit law was several times amended in order to fill the regulatory gaps or rectify the liberal legislation existing before the crisis.

4. When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?

The changes have mostly occurred starting with 2011 after the new Government was installed. These reflect the Hungarian way to address the economic and social consequences of the consumer credit crisis.

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spending? (For example: has there been practice of selling risky financial services and products, ie with regard to savings?)

Risky financial services sold to the Hungarian consumers constitute the very heart of the Hungarian case of over-indebtedness. Loans denominated in foreign currencies in particular have been debated for years. Consumers and lawyers considered that in such cases the bank does not provide a foreign exchange service for the consumers, but only records the loan in a foreign currency. The *Kásler* ruling of the CJEU provides now the legal basis for the Hungarian courts to clarify this question, and also the Kúria is committed to bring this debate to an end. Although it was on the agenda of the case law unification decision of the Kúria, the decision issued on June 16, 2014 did not tackle this issue. Consequently, it will be clarified by future legislative measures since it is a matter of regulatory law rather than of contractual justice to be rendered by the judiciary.

ICELAND

M. Elvira Méndez Pinedo and Irina Domurath[1]

Preliminary Information

- Data collection and sources

Together with relevant information from the Statistical Office Iceland (Statistics Iceland),[2] this study is largely based on publicly available data published in reports issued by the Central Administration (such as the April 2013 Report of the Ministry of Presidency on consumer protection in financial markets), other Ministries, the Central Bank of Iceland,[3] and documents published by other international institutions between 2008-2013,[4] as well as selected information about cases litigated before the Supreme Court of Iceland. We interviewed ten randomly selected consumers with mortgages in order to obtain information for Sections XI and XII. Anecdotal evidence is given in order to fill gaps.

Complete and coherent presentation of data is complicated by the **different data collection methodologies** employed by different institutions. We decided to mainly use data from the Central Bank and "Statistics Iceland", the statistical data collection office in Iceland. The Central Bank of Iceland was responsible for data collection on this issue from 2009 to 2012. Since 2012 this competence has been given to Statistics Iceland. The Central Bank uses primary data from tax authorities combined with primary data provided by financial institutions. Statistics Iceland analyses household debt through two different methodologies: one analysis with tax return data, based on factual data and represented as such, and another independent analysis based on household surveys which is estimated and represented as such. Thus, the diverse methodologies provide different numbers and ratios. The different methodologies, however, rely on a similar definition of "household" and tend to overestimate the number of individuals and underestimate the number of nuclear families (individuals older than 16 are represented as independent households although they may still live with their parent(s)).

Essential information concerning the status of EU acquis and EEA consumer law in Iceland as well as Iceland´s negotiating position was published on the occasion of the Intergovernmental Conference between Iceland and the EU on 30 March 2012. Negotiations on Chapter 28 (consumer protection) began and ended on the same date as no particular problems concerning the incorporation of the EU

1 The authors thank Gudmundur Ásgeirsson and Sigurdur Sigurdsson for their valuable assistance in the data collection. They also thank María Thejll for research assistance.

2 A legal statute (Lög no. 163/2007) gave the Icelandic Statistics Office ("Statistics Iceland") the competence to collect statistical information about different private issues of public relevance for society.

3 Central Bank of Iceland Working Paper No. 59 "Households' position in the financial crisis in Iceland" by Thorvaldur Tjörvi Ólafsson and Karen Áslaug Vignisdóttir, June 2012 (Central Bank Report WP 59)

4 Important background information, especially concerning this study can be found in the Report of the Special Investigation Commission appointed by the Icelandic Parliament to investigate and analyse the causes leading to the collapse of the three main commercial banks in Iceland (Icelandic Parliament, 2010). Summaries in English can be found here: http://www.rna.is/eldri-nefndir/addragandi-og-orsakir-falls-islensku-bankanna-2008/skyrsla-nefndarinnar/english/. All information referring to the operation of the financial markets, behaviour of the banks, regulatory framework and policy, as well as relevant EEA law applicable before 2008, is to be found there as well as the emergency measures adopted by the authorities and Parliament after the crisis. This research has been confirmed by later documents of the Administration and the new public policy regarding the regulation of the financial markets. The assistance programme from the IMF has formally finalised in 2011, but it continues to monitor the situation in Iceland, see IMF, Country reports on Iceland, 2012 and 2013).

acquis were noted.[5] Negotiations regarding accession were suspended by the Icelandic government after the last general election held on April 2013. At the time of writing it is uncertain whether or not the Parliament will officially put an end to this accession process.

- Personal disclaimer for Prof. M. Elvira Mendez Pinedo (MEMP)

MEMP was involved in the litigation before the Supreme Court on illegal FX-indexed loans (cases 604/2010 and 600/2011 concerning debt-relief). She has also carried out legal research on the legality of CPI-indexation in European law.[6] She disclosed provisional findings to the Icelandic Parliament, to the public - while the incorporation of Directive 48/2008 was being carried out - and to the Committee on Consumer Protection in Financial Markets. Moreover, regarding the legality of Icelandic practice MEMP sent three letters to the European Commission, EFTA Surveillance Authority (ESA) and European Parliament.

- Basic numbers

In February 2013 Iceland had a population of 321,857 inhabitants and 325,000 in 2014. The increase in population should be taken into account when analysing the levels of indebtedness. It is difficult to establish percentages due to the fact that data varies according to different parameters: households or families. According to Statistics Iceland, Iceland had 189,095 households in 2012. This number can vary when data provided by the Central Bank is used. Tax authorities report that 264,193 tax declarations were presented for the year 2012.[7]

Table 1: Iceland – number of households

Population - key figures 1703-2013

	Population 1 January
2000	279,049
2001	283,361
2002	286,575
2003	288,471
2004	290,570
2005	293,577
2006	299,891
2007	307,672
2008	315,459
2009	319,368
2010	317,630
2011	318,452
2012	319,575
2013	321,857

Latest update: 2013-02-12
Source: Hagstofa Íslands, Hagskinna
Unit: Number
Reference time: 1703-2013

Source: Statistics Iceland 2013 Report "Wages, income and labour market – household finances 2012"

5 Ministry of Foreign Affairs, Information site on the negotiations with the EU, Chapter 28 at http://eu.mfa.is/negotiations/chapters/28/).

6 The cost of credit in Iceland under European judicial review: may legality and transparency justify unfairness? forthcoming ERT, 2014, pp. 303-329.

7 Both the official Census in Iceland (in 2014 estimated 141,834 families) and the numbers estimated by the tax authorities (145,137 families) divert from this "over-estimation" of families. In July 2014, according to Statistics Iceland the Icelandic population consists of 81,380 families and 60,454 persons not in family nucleus. Most of the families are families with children. The number of families with at least one child younger than 25 was 54,222 and 22,444 families consisted of couples without any children. There were 118,617 private households according to the Census with 307,398 persons which corresponds to 2.59 individuals on average in each private household. In addition 7,397 persons were living in institutional households and 761 were homeless or not living in a private household, but category not stated. Information at http://www.statice.is/Pages/444?NewsID=10938.

Table 2: Population Iceland

Tafla 1. Fjöldi og meðalstærð heimila á Íslandi
Table 1. Number of households and mean household size in Iceland

	2007	2008	2009	2010	2011	2012	2012
Fjöldi heimila *Number of households*	117.900	121.900	126.100	124.600	122.900	123.900	± 4.700
Meðalfjöldi á heimili *Mean number of household members*	2,5	2,5	2,4	2,4	2,4	2,4	± 0,05
Meðalfjöldi 16 ára og eldri *Mean number 16 years and older*	1,9	1,9	1,9	1,9	1,9	1,9	± 0,03
Meðalfjöldi yngri en 16 ára *Mean number younger than 16*	0,6	0,6	0,6	0,6	0,6	0,6	± 0,03

Source: Statistics Iceland

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

The terms "indebtedness" and "over-indebtedness" are **not defined** in the national legal framework. However, we can infer an understanding from the sources and data used. The term "indebtedness" usually refers to any the situation arising from taking on loan obligations; "over-indebtedness" is reflected in the terms of "distress", "arrears", "payment difficulties", and "difficulty to make ends meet". The Central Bank Report WP 59 defines households as being in distress "if their total spending on debt payments and necessary minimum living expenses (taking the added margin into account) exceeds their disposable income."[8] The Central Bank refers to those that use more than 40 per cent of disposable income to pay off loans.[9] It is our understanding that this threshold is rather high in comparison with other countries.

2. *Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?*

The term is not defined in the Icelandic legal order. However, some legislation uses the term explicitly or implicitly, albeit without defining it.[10] According to MP Sigrídur Ingadóttir, the Icelandic Parliament has been struggling with that issue. So far a definition of this concept and a pragmatic solution has not been reached. The Central Bank Report considers a simultaneous combination of "financial distress and negative housing equity" as making homeowners "vulnerable".[11] In this regard, both middle-income families with children (many of which had foreign-denominated loans), and low-income unmarried individuals seem especially "vulnerable".[12] The Debtor´s Ombudsman also uses this double criteria.

3. *Is the term "poverty" or "low-income consumer" defined in the national legal order?*

The term is not defined in the Icelandic legal order. Indirectly and in a legally non-binding manner the Ministry of Welfare uses reference parameters of necessary "minimum consumption" for social

8 Central Bank Report WP 59, p20.

9 ÞTO&KAV:2009; The Debtor's Ombudsman uses the guidelines from 2011 in order to determine "over-indebtedness", leaving out housing and transportation cost, as those are to be determined on a case by case basis.

10 For examples see Central Bank Report WP 59, pp 79 and 83.

11 Central Bank Report WP 59, p6.

12 *Ibid.*

assistance or public pension purposes. It is currently 291,000 ISK for an individual, around 1,860 EUR as of 31 March 2014. The Ministry of Welfare and the Debtor's Ombudsman use guidelines to calculate minimum amounts essential for living and, on that basis, provide further assistance or calculate right to debt-relief or restructuring.

Statistics Iceland operates a "at-risk-of-poverty" threshold, which is defined as "60% of the median equivalised disposable income". Equivalised disposable income depends on the disposable income of the household and how many people are living from that income. For instance, two adults with two children need 2.1 times more disposable income than a person who lives alone in order to have comparable disposable income. The at-risk-of-poverty rate in Iceland was for instance 9.8% in 2010.[13]

II. Numbers on over-indebtedness

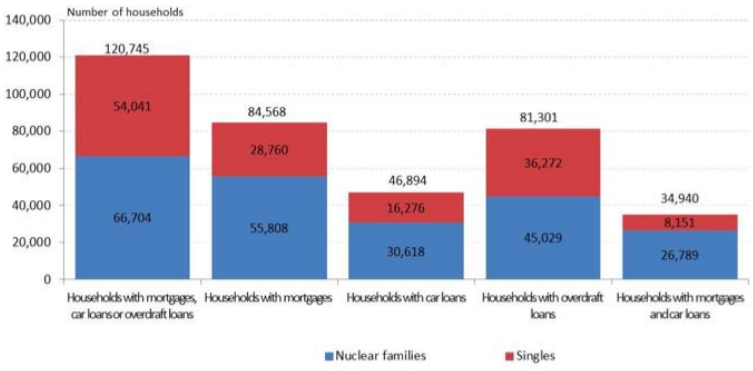
4. How many consumers are considered "indebted" in the country? (since 2000)

According to the Central Bank, in the year 2012 there were 120,745 households with some kind of loan (mortgage, car loan, or overdraft). Statistics Iceland states that 154,694 families had some form of debt in 2012, in contrast to 92,759 families in 2000.[14] These families have any kind of debt, e.g. mortgage debt, motor vehicle debt, overdraft, credit card debt, student loan, etc.

Given the number of 189,095 households in Iceland in 2012 (Statistics Iceland) – **81.8% of all Icelandic families**, or 38.59% of the total population (including children) have debt of some sort. Without the children, the Central Bank refers to a level of indebtedness of 68% in general but 90% for "nuclear families" (see Table 4).

Table 3 - Numbers of indebted households in total by type of debt – "nuclear families" (households consisting of single parents and their children, couples without children, and couples with children) and singles

Figure 3.1a
Number of indebted households in total by type of debt divided into nuclear families and singles[1]



1. All loans backed by real estate as collateral are defined as mortgages. Nuclear families are couples with and without children and single parents.
Source: Central Bank of Iceland Household Sector Database.

Source: Central Bank WP 59, 2012.

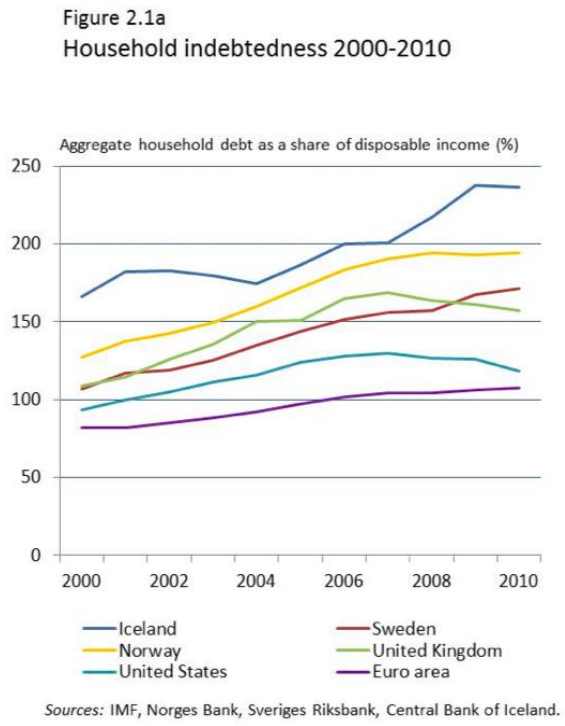
13 http://www.statice.is/ (EN)

14 According to a statement obtained from Statistics Iceland, it "overcounts" families, as many individuals older than 16 years still live with their parents and the census correction does not deliver accurate results.

Statistics Iceland provides the following data, using the data from the Icelandic tax authorities (solely based on tax returns) (www.statice.is):

Year	Nr of households	Average debt in million ISK
2000	92,759	5.2
2001	94,512	5.9
2002	96,552	6.2
2003	99,659	6.8
2004	100,230	7.8
2005	101,883	9.3
2006	105,538	10.9
2007	109,571	12.8
2008	106,728	16.4
2009	142,639	14
2010	153,320	13
2011	150,525	12,5
2012	154,694	12,4

Table 4 –Household indebtedness 2000-2010



Source: Central Bank Report WP 59

International comparison shows that levels of indebtedness as aggregate household debt as share of disposable income were higher in Iceland than in other countries.

a. How many consumers have mortgage debt?

According to the Central Bank Report 84,568 households have mortgage debt.[15]

b. How many consumers have motor vehicle debt?

According to the Central Bank Report 46,900 households have motor vehicle debt.[16]

c. How many consumers have other debt (credit card, general consumption)?

According to the Central Bank Report 81,301 households had overdraft loans.[17] Data on other forms of debt is only available with regard to over-indebtedness, see below.

d. What *percentage* of those "indebted" consumers / households is:

i) single / married

According to information received from Statistics Iceland, which assumes a total of 154,694 indebted families in 2012, there were 76,464 indebted individuals. Marital status is not a relevant parameter in the data collected in Iceland, as the information collected comes from the tax declarations that ignore this parameter. Instead "economic units" (individuals / marriage & partnership, with or without children) is the concept used. The Central Bank does not collect any data using these parameters.

ii) with / without children

Data from Statistics Iceland provide the following data: 14,748 single parents are indebted, 32,000 couples without children, and 31,482 couples with children.

iii) with / without work

No data available.

iv) Retired

No data available (tax authorities only take account of "age" as a parameter).

v) Low-income consumers

A correlation between indebtedness and income has not yet been part of the data collection in Iceland. However, the Central Bank establishes that middle-income families with children, most of which had foreign-denominated loans, and low-income singles seem especially "vulnerable".[18]

According to Statistics Iceland,[19] in the year 2012, out of the total group of 189,095 households taken into account for the study, the lowest 10% (1st decile) had a total disposable income (in other words total Annual Income minus Total Taxes and Total Interest Expense) of 4,497,000 ISK per year. By comparison, the next group (2nd decile) had a disposable income of 21,184,000 ISK and the top group (10th decile) had a disposable income of 226,285,000 ISK.

5. How many consumers are considered "over-indebted" in the country? (since 2000)

Measurement of "over-indebtedness" is difficult given the lack of a clear-cut definition. Statistics Iceland provides for data on "households in financial difficulties" since 2004. The most recent data relates to 2012. The term "financial difficulties" is used and in various different situations ranging from arrears on mortgage or rent payments to "difficulty to make ends meet".

15 Central Bank Report WP 59, pp 15 and 16.

16 Central Bank Report WP 59, p16

17 Central Bank Report WP, p15.

18 Central Bank Report WP 59, abstract.

19 www.statice.is, table on Assets and liabilities of households 2000-2012.

Table 5

Source: Statistics Iceland (http://www.statice.is)

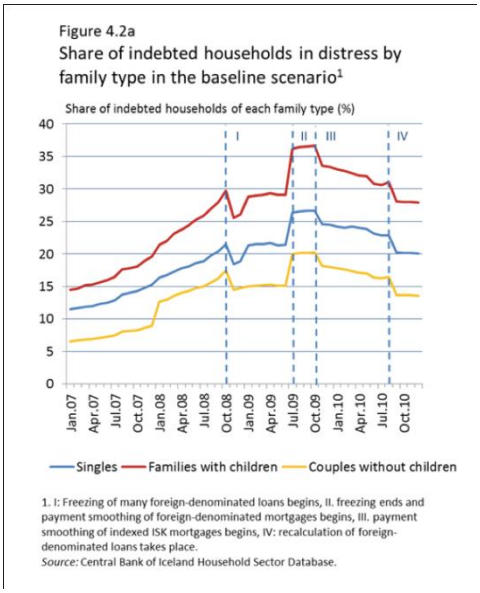


Table 6 – Households in distress

Source: Central Bank Report WP 59, p. 36.

Households in financial difficulties by household type, 2004-2012

	Percent, %								
	2004	2005	2006	2007	2008	2009	2010	2011	2012
Total									
Arrears on mortgage or rent payments	9.4	8.0	5.7	5.8	5.5	7.1	10.0	10.1	10.1
Housing cost is a heavy burden (older definition)	12.4	11.6	9.9	9.6	11.8	15.0	16.4	19.2	.
Housing cost is a heavy burden	.	.	.	.	.	.	29.1	31.7	27.3
Arrears on other loans	10.7	7.9	5.8	8.4	5.5	10.3	13.1	12.3	10.4
Payments of other loans is a heavy burden	9.7	9.7	7.6	11.5	10.3	15.5	19.1	15.1	13.9
Unable to meet unexpected expences	36.1	38.0	31.9	29.8	26.9	29.8	35.6	39.8	35.9
Difficult to make ends meet	46.2	36.8	34.8	28.4	30.1	39.0	48.7	51.5	48.2

The Central Bank looks at this issue from a different angle. The share of "indebted households in distress" in connection with the debt relief measures taken, which we will come back to later as well as family types – is illustrated in Table 5. We can see that since October 2008 (when the financial crisis hit Iceland) the percentage of indebted households that are considered "in distress" has been between 25% and 37%. The Central Bank Report WP 59 summarises the situation of over-indebtedness of households after the financial crisis in the abstract as such: (bold highlights by rapporteurs of this study):

"[…] The analysis suggests that the **share of indebted households in distress grew from 12,05 per cent in early 2007 to 23,05 per cent** on the eve of the banking collapse in the autumn of 2008, when the lion's share of the balance sheet shocks had already taken place. The **extent of acute distress nearly quadrupled** over the same period. Forbearance efforts provided temporary breathing space, but the **share in distress is estimated to have peaked at 27,05 per cent in autumn 2009, before declining to 20 per cent at year- end 2010 due to policy and legal interventions**. … The incidence of **negative housing equity increased dramatically, from roughly 6 to 37 per cent** of indebted homeowners, over the four-year period. Negative housing equity is more widespread among high-income than low-income households. The share of homeowners simultaneously in distress and negative equity rose from roughly 1 to 14 per cent but declined to 10 per cent by the end of the period. …"

a. How many individual consumers / households are behind (up to 3 months and more than 3 months) with the repayment of:

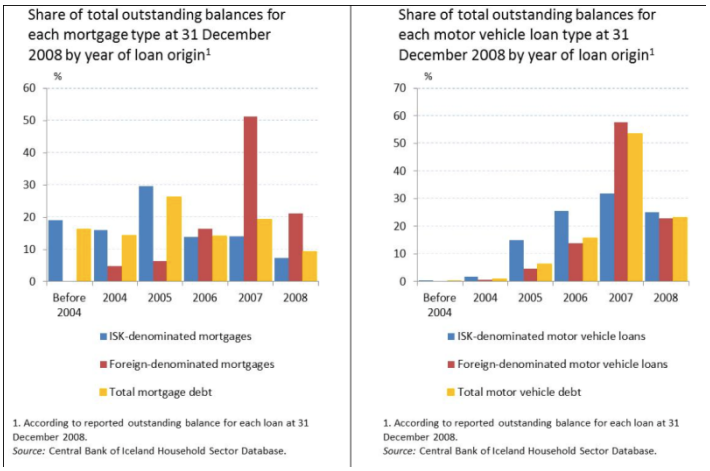
i) General consumption loans

Statistics Iceland provides for data with regard to "other loans" in general. As can be seen in Table 7 in 2012, 10.4% of households were in "arrears on other loans" and 13.9 % considered payments of other loans a "heavy burden". According to information from the Central Bank and the Ministry of Finance, there were 27,248 individuals in the Registry for default payments when 90 days in delay concerning an amount of more than 40,000 ISK).[20] According to the same data, the percentage of borrowers in default went down from 22% in May 2012 to 16% in 2012.[21]

ii) Motor vehicle loans

As Table 7 shows, the share of outstanding balances for motor vehicle loans peaked at just over 50% in 2007 before going down to about 22% in 2008. The vast majority (around 70%) of the total outstanding balance of FX-denominated motor vehicle debt was issued in 2007 and early 2008, thus reflecting the increase in foreign-currency borrowings in the last two years before the banking collapse in autumn 2008.[22]

Table 7: share of outstanding mortgage and motor vehicle loans, 2008



Source: Central Bank Report WP 59, p17.

iii) Student loans

There is no data available on student loans, even though they also represent a major debt issue for many Icelanders. The latest Report from the Icelandic Student Loan Fund LÍN refers to 31,000 student loans in their portfolio. Between 2011 and 2012 LÍN supported circa 20,000 active students.

iv) Credit card debt

There is no data available on mortgage debt. Usually, it should be included in the numbers on debt other than mortgage or rent payments.

v) Mortgages / housing loans

20 Ministry of Welfare "Greinargerð um fjárhagsstöðu heimilanna", April 2013, p18.

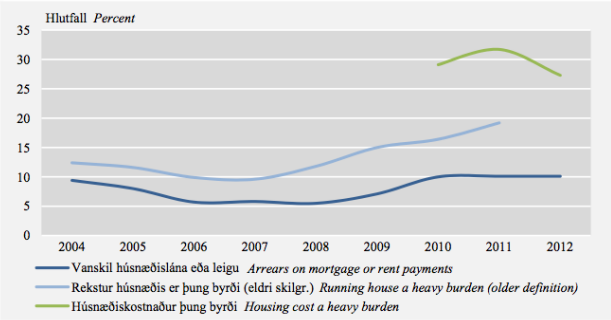
21 Ministry of Welfare "Greinargerð um fjárhagsstöðu heimilanna", April 2013, p17.

22 Central Bank Report WP 59, page 16.

According to Table 5, 10.1% of households were in "arrears on mortgage or rent payments". With regard to payment problems related to housing, Statistics Iceland data suggests that the number of households in arrears on mortgage and other rent payments doubled between 2009 and 2010 – in the immediate aftermath of the financial crisis.

Table 8

Mynd 1. **Þung byrði og vanskil húsnæðislána eða leigu**
Figure 1. *Heavy burden and arrears on mortgage or rent payment*



Skýringar *Notes*: Öryggisbil (95%) 2012: Vanskil húsnæðislána eða leigu ±1,3, húsnæðiskostnaður þung byrði ±1,9. *CI (95%) 2012: Arrears on mortgage or rent payments ±1.3, housing cost is a heavy burden ±1.9.*

Source: Statistics Iceland, Statistical Series 2013:3 "Wages, Income and labour market – household finances", April 2013

The Report from the Administration on financial difficulties of the households published in 2013 also provides data on this question,[23] but offers a more favourable trend in the last years. The number of families with negative equity on their homes (i.e. those who owed more than the registered/market value of the property) remained stable until year 2007 around 5,000-7,000 households. After the financial crisis this increased to 25,000 (by the end of 2010). In 2011 this figure went down to 21,000 households, and further down in 2012 to 17,780.[24] In 2013 the authorities expected a rapid decrease in this figure following recalculation of illegal FX-indexed loans and effect of several debt-mitigation and fiscal public policies implemented in 2011 and 2012.

vi) interests

No data available.

b. How many individual consumers / households have initiated bankruptcy proceedings?

Bankruptcy declarations increased in the years 2011 and 2012 compared with the years 2005-2010 although the numbers are considerably lower than the years 2001-2004. 274 individuals have initiated bankruptcy proceedings in 2012, of which 103 are women and 171 men. With regard to women there was a big jump between 2011 (24 women) and 2012 and a steady increase since 2001 (with a "bump" in 2002 with 115 women), whereas with regard to men, the numbers have been more than 100 since 2001, peaking in 2002-2003 with 252-293 insolvencies.

23 Ministry of Labour and Innovation, financial and economic affairs, Ministry of Presidency, Ministry of internal affairs and Ministry of Welfare, Analysis on financial situation of households, 2013, 8, 18-19.

24 http://www.statice.is/pages/2980.

Table 9: Number of bankruptcies women (konur), men (karlar),

Tafla 7: Fjöldi gjaldþrotaúrskurða á landinu öllu, 2001–2012.

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Meðaltal
- Konur	81	115	96	55	35	26	35	38	13	18	24	103	53
- Karlar	217	252	293	220	160	89	118	163	99	121	162	171	172

Heimild: Dómstólaráð.

Source: Ministry of Welfare[25]

The decline in bankruptcy proceedings could, for example, be explained by the recent changes in bankruptcy law that allow for discharge of debt after two years – this is not a very attractive option for creditors. In fact, "unsuccessful executions" have replaced bankruptcy proceedings as the creditor can keep the debtor in a state of permanent debt (under this procedure any financial gain of the debtor can lead to the enforcement proceedings being initiated once more and the gain collected). This presents a loophole in the new bankruptcy law as creditors are having recourse to a practice that was widespread under the old bankruptcy law. In the beginning of 2014, there were 14,950 individuals in Iceland with the status of "unsuccessful execution" of financial claims in the credit databases.[26]

c. How high is the average amount of outstanding debt?

According to the latest tax reports for 2013, Icelandic households had a total debt of 1,785,000,000,000 ISK. Divided by 145,137 families the average debt is 12,298,725 per household. The Debtor's Ombudsman observed that the average debt has been decreasing in recent times (interview). Those seeking assistance from the Debtor's Ombudsman had an average debt of 33 million in 2010, 22.3 million in 2011, 21.2 million in 2012 and 18.5 million in 2013.

The latest data from Statistics Iceland is slightly different, but provide a similar picture. The average debt per family in Iceland is 10.2 million ISK and average mortgage per family is 6.5 million ISK. Here we take into account the entire population. If we take into account only those indebted, the average debt is 12.4 million ISK. 76,464 Individuals owe on average 6.5 million ISK, 14,748 single parents owe in average 11.6 million ISK, 32,000 couples without children owe in average 14.3 million ISK and 31,482 couples with children owe in average 25.4 million ISK.[27]

d. What percentage of those "over-indebted" consumers / households (a, b) are:

i) single / married

In Table 8 we already saw that single households fare better than families with children, but worse than couples without children. Central Bank data suggests the same.[28] Single women living alone have less payment difficulties, both with regard to mortgage and rent payment as well as other loans.

25 Ministry of Welfare "Greinargerð um fjárhagsstöðu heimilanna", April 2013, p 20, Table 7.

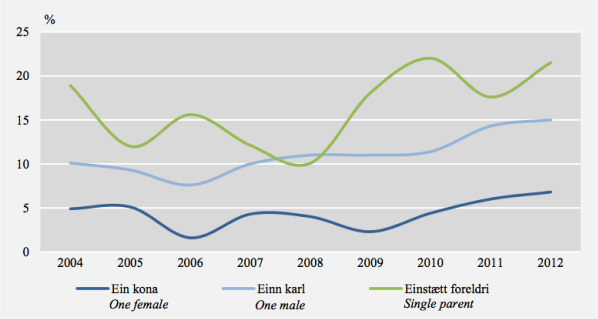
26 http://skuldavandi.com/2013/03/19/arangurslaust-fjarnam-ur-leik-fyrir-lifstid/.

27 www.statice.is.

28 Central Bank Report WP, p36, Figure 4.2a.

Table 10 – payment difficulties concerning housing among single households

Mynd 5. **Vanskil húsnæðislána/leigu meðal heimila þar sem einn fullorðinn býr**
Figure 5. *Arrears on mortgage or rent payments among single adult households*



Skýringar *Notes*: Öryggisbil (95%) 2012: Ein kona ±3,5, einn karl ±4,6, einstætt foreldri ±6,4. *CI (95%) 2012: One female ±3.5, one male ±4.6, one parent ±6.4.*

Source: Statistics Iceland Statistical Series 2013:3 "Wages, Income and labour market – household finances", April 2013

ii) with / without children

Households with children are more likely to experience payment difficulties than childless households. Between 2007 and 2009 the percentage of families with children "in distress" rose dramatically from 14.5% to 36.5%, then declined in 2010 to about 28%.[29] The numbers for childless couples are lower than that. In 2007, only 6.5% of households of childless couples were "in distress", peaking in 2009 at 20.5%, and declining to 13.5%.[30] Also Table 8 (data from Statistics Iceland) shows that couples with children are more affected by over-indebtedness than couples without children. Statistics Iceland also states that households with single parents form the demographic group that are in the most "financial difficulties". In this group 21.5% have had difficulties with mortgage or rent payments in 2012 and 22.3% with other loans. 73.4 % state to have difficulties to make ends meet and 68% of the single parents claim to have difficulties to meet unexpected expenses.

Table 11 – arrears of mortgage or rent payments among different household types

	Hlutfall *Rate*							Öryggis-bil *CI*	Áætlaður fjöldi *Estim. number*
	2006	2007	2008	2009	2010	2011	2012	2012	2012
Vanskil húsnæðislána eða leigu									
Arrears of mortgage or rent payments									
Alls *Total*	**5,7**	**5,8**	**5,5**	**7,1**	**10,0**	**10,1**	**10,1**	**± 1,3**	**12.100**
Heimili án barna *Households without dependent children*	3,8	4,9	5,0	5,5	7,1	8,3	7,7	± 1,6	5.500
Einn á heimili *One person households*	4,8	7,4	7,8	6,8	8,0	10,3	11,0	± 2,9	4.000
Einn á heimili, kona *One person household, female*	1,6	4,3	4,0	2,3	4,4	6,0	6,8	± 3,5	1.200
Einn á heimili, karl *One person household, male*	7,6	10,0	11,0	11,0	11,4	14,3	15,0	± 4,6	2.800
Fleiri en einn fullorð. án barna *More than one adult without childr.*	2,9	2,6	2,3	4,1	6,1	6,2	4,4	± 1,3	1.500
Heimili með börn *Households with children*	8,2	7,0	6,2	9,5	14,0	12,9	13,5	± 2,0	6.600
Einstætt foreldri með barn eða börn *Single parent with one or more dependent children*	15,6	12,1	10,1	18,1	22,0	17,6	21,5	± 6,4	2.200
Tveir fullorðnir, eitt barn *Two adults, one dependent child*	6,8	4,2	4,2	7,5	11,2	9,5	10,1	± 3,2	1.200
Tveir fullorðnir, tvö börn *Two adults two dependent children*	4,7	5,9	4,9	8,0	10,3	12,2	11,3	± 3,2	1.500
Tveir fullorðnir, fleiri börn *Two adults three or more children*	8,5	9,0	9,1	8,0	16,8	13,8	14,4	± 4,2	1.200
Fleiri en einn fullorð. með börn *More than one adult with children*	6,7	6,0	5,4	7,8	12,1	11,8	11,4	± 1,8	4.400

Source: Statistics Iceland Statistical Series 2013:3 "Wages, Income and labour market – household finances", April 2013

29 Central Bank Report WP 59, p35.

30 Central Bank Report WP 59, p37.

With regard to "arrears with mortgage and rent payment", Statistics Iceland provides that in 2012 there were 10.1% of households without dependent children in such difficulty, compared to 13.5% of households with children.[31] All in all, also with reference to question 5 lit) d-iv (below), young households with children that took mortgages late in the housing boom are considered a particularly hard-hit group. Already before the crisis (January 2007) 21.5% of those households were already in distress. In mid-2009 this share was nearly 47%, with the number dropping slightly to 35.5% at the end of 2010.[32]

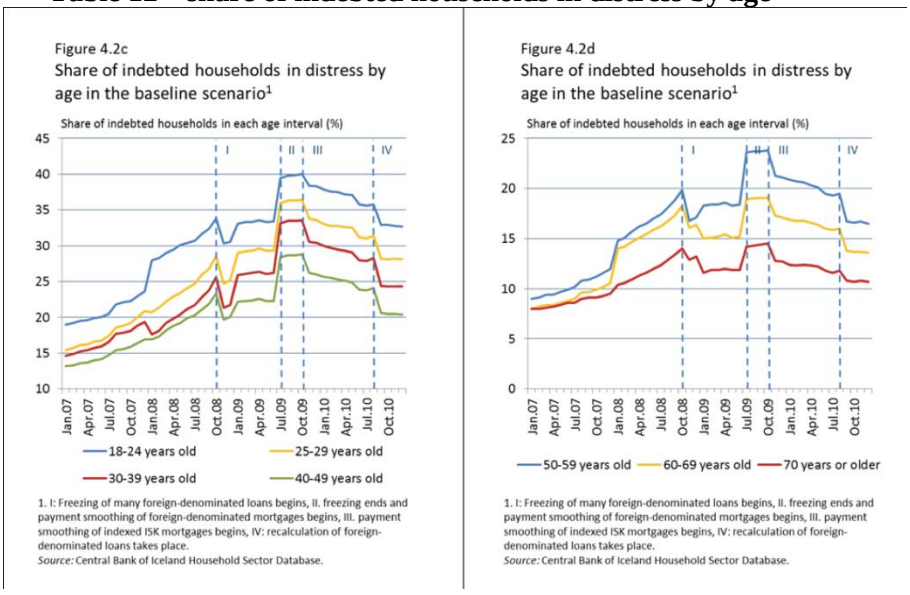
iii) with / without work

No data available.

iv) Retired

Central Bank data on "households in distress" by age (not retirement) suggest that older households groups experience less difficulty than younger households. Young homeowners in the 25-29 age group are considered most "vulnerable" by the Central Bank. Accordingly, distress is inversely related to age.[33] This can probably be explained by the participation of younger people in the housing boom, while older people maybe inherited their property or have been further along in the repayment of their mortgages when the crisis hit. Contrasting data seem to have been the basis for the assessment of the Ministry of Welfare, which assumes that households with average age of adults is 30-39 years have most difficulties.[34]

Table 12 – share of indebted households in distress by age



Source: Central Bank Report WP 59, p36.

Data provided by Statistics Iceland state that people between 30 and 39 are the ones that have mostly experienced increasing financial difficulties with regard to housing costs.

31 Statistics Iceland Series 2013:3 "Wages, Income and labour market – household finances", April 2013.

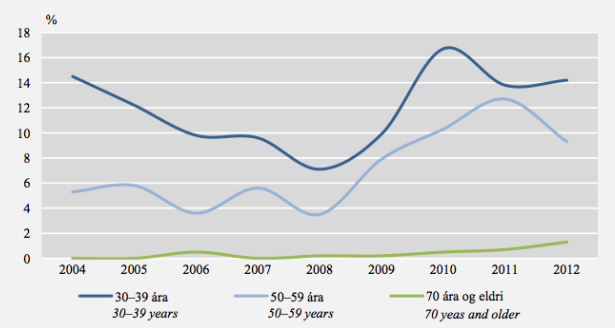
32 Central Bank Report WO 59, p37.

33 Central Bank Report WP 59, p59.

34 Ministry of Welfare Press Release http://www.velferdarraduneyti.is/frettir-vel/nr/33814.

Table 13 – arrears on housing loans or rent among different age groups

Mynd 7. **Vanskil húsnæðislána/leigu lána meðal ólíkra aldurshópa**
Figure 7. *Arrears on housing loans or rent among different age groups*



Skýringar *Notes*: Öryggisbil (95%) 2012: 30–39 ára ±3,0, 50–59 ára ±3,1, 70 ára og eldri ±1,4. *CI (95%) 2012: 30–39 years ±3.0, 50–59 years ±3.1, 70 years or older ±1.4.*

Source: Statistics Iceland Statistical Series 2013:3 "Wages, Income and labour market – household finances", April 2013

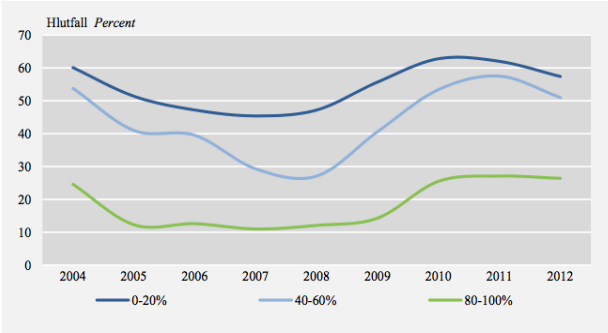
v) low-income consumers

In general, low-income consumers are in greater difficulty than high-income consumers. Distress is inversely related to income quintiles. The lower the income quintile, the higher the percentage of households in distress, both before and after the crisis. According to the Central Bank, in October 2010, these were around 47% in the lowest income quintile group, 20% in the middle income quintile, and only 2% in the highest income quintile group.[35] Similar conclusions can be drawn from a press release of the Ministry of Welfare on the basis of information published by Statistics Iceland in 2012.[36]

A similar picture emerges when looking at data provided by Statistics Iceland. At the end of 2010, 46-47% of those households situated at the lower income quintile had financial difficulties compared to only 3-4% in the highest-income quintile.

Table 14

Mynd 9. **Möguleikar heimila á að ná endum saman eftir tekjufimmtungum**
Figure 9. *Ability of households to make ends meet by income quintiles*



Skýringar *Notes*: Öryggisbil (95%) 2012: 0–20% ±4,9, 40–60% ±4,4, 80–100% ±3,5. *CI (95%) 2012: 0–20% ±4,9, 40–60% ±4,4, 80–100% ±3,5.*

Source: Statistics Iceland, Statistical Series 2013:3 "Wages, Income and labour market – household finances", April 2013

35 Central Bank Report WP 59, pages 34 and 36.

36 http://www.velferdarraduneyti.is/frettir-vel/nr/33814.

III. Numbers on evictions

1. How many evictions have there been per year since 2000 (or later if earlier data not available)?

Data relating to the enforcement of mortgage agreements can be found at the "Statistics Iceland" database, but only concerns the years before the financial crisis. Between the years 2000 and 2007 the numbers on evictions were: 176, 235, 248, 287, 290, 253, 231, and 234.[37]

In a recent reply from the Minister of Interior to Member of Parliament Arni Páll Árnarsson we find the total number of evictions during the period 2008-2013 (8,694 properties, 4,730 from individuals and 3,964 from small companies).[38] In contrast, a Report published by several ministries in Iceland shows that the number of enforced credit agreements has actually gone down from 36,377 in 2003 to 17,202 in 2012 and the number of forced sales was stable around 1,041 in 2003 to 979 in 2012.[39] This is probably due to the moratorium on evictions.

Table 15 – number of enforced credit agreements

Tafla 6: Fjöldi fullnustugerða 2003–2012.

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Stofnuð aðför	36.377	30.150	23.165	24.582	25.036	25.218	26.236	21.158	18.741	17.202
Árangurslaust fjárnám	5.544	6.264	5.570	4.869	5.595	5.734	6.875	8.373	16.324	10.317
Beiðni um nauðungarsölu -fyrsta fyrirtaka	7.776	7.383	4.847	4.630	4.726	5.078	4.598	4.786	5.707	5.306
Nauðungarsala - afsal/seldar eignir	1.041	721	421	408	463	587	756	1.427	685	979
Þar af íbúðarhúsnæði	*496*	*291*	*140*	*111*	*172*	*327*	*404*	*1.117*	*485*	*773*

Heimild: Atvinnuvega- og nýsköpunarráðuneyti.

Source: Ministry of Welfare, http://www.velferdarraduneyti.is/rit-og-skyrslur-vel/nr/33807

2. How many evictions took place because of:

a. Unpaid mortgage instalments?

b. Unpaid monthly rent?

In Iceland, there is no distinction made for statistical purposes between those parameters.

3. Who are the persons affected (percentage of young people, families, old people, unemployed)?

We could not obtain data on persons affected by evictions. However, assuming a positive correlation between persons affected by over-indebtedness and persons affected by evictions (evictions being a possible consequence of over-indebtedness) and considering that payment difficulties affect more young (less than 40 years old) than older people, single parents, men, and low-income households with children (see above), then those groups of consumers should then also be more affected by evictions than other groups of consumers.

37 www.statice.is.

38 http://www.mbl.is/frettir/innlent/2014/05/16/8_694_fasteignir_bodnar_upp_fra_2008/.

39 Greinargerd um fjárhagsstödu heimilanna, April 2013, available at : http://www.velferdarraduneyti.is/rit-og-skyrslur-vel/nr/33807

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

The following statues constitute the applicable legal framework in Iceland to most cases of over-indebtedness:

- Act on interest and Indexation no. 38/2001 (*Lög um vexti og verðtryggingu*, nr. 38/2001) adopted 26 May 2001.
- Act on injunctions and court proceedings in order to protect consumers general no. 141/2001 (incorporating Directive 98/27/EC) with various notifications (ie. Notice nr. 1320/2011 on associations being recognised locus standi for the defense of the public interest).
- Act on financial undertakings no. 161/2002 (*Lög um fjármálafyrirtæki*, nr. 161/2002) adopted 20 December 2002.
- Act on distant selling of financial services no. 33/2005 (incorporation of Directive 2002/65/EB)
- Act on supervision of commercial and marketing practices no. 57/2005 and subsequent regulations (incorporation of Directive 98/6/EC on consumer protection in the indication of the prices of products and Directive 2005/29/EC on prohibition of abusive commercial and advertising practices).
- Act on debt collection no. 95/2008 (*Innheimtulög*, nr. 95/2008) adopted 12 June 2008.
- Regulation on maximum collection costs no. 37/2009 (R*eglugerð um hámarksfjárhæð innheimtukostnaðar* nr 037/2009) adopted 21 January 2009.
- Act on contracts, agency and void legal instruments no. 7/1936 with later amendments (ie. Incorporation of provisions from Directive 93/13/EC) (*Lög um samningsgerð, umboð og ógilda löggerninga, með síðari breytingum* nr. 7/1936) adopted/entered into force 1 February 1936 last modified 30 September 2011).
- Act on consumer loans no. 33/2013 (*Lög um neytendalán* nr. 33/2013 reforming the previous Act on consumer loans or lög no. 121/1994 from 21 September 1994 which incorporated previous Directive 87/102/EC). It was adopted on 27 March 2013 and it entered into force on 1 November 2013. This act implements the CCD into the Icelandic legal order.

1. Is the CCD 2008/48 implemented into national law?

Yes. The CCD 2008/48 has only been recently implemented into national law through the Act on consumer loans no. 33/2013. The EFTA Court had declared that Iceland has violated the EEA Agreement for the late incorporation of EEA legislation into its national legal order.[40] Although Iceland is not a EU member state, EU consumer *acquis* has been incorporated into Iceland since 1994 due to the European Economic Area Agreement (EEA) which entered into force on the 1 January 1994.

2. Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?

Act no. 33/2013 includes mortgages within its scope of application. The legislation goes also beyond EU by limiting maximum annual interest rate on credit (50 times the legal interest of money regularly calculated and published by the Central Bank).[41] The maximum interest ban will especially affect "small loans" where recent abuses have been denounced to authorities.

40 EFTA Court, judgment of 15.5.2013, case E-12/12 *EFTA Surveillance Authority v Iceland*, not yet reported.

41 Art. 26 Act No. 33/2013.

3. With regard to the Mortgage Credit Directive, will there have to be an adjustment of national law? What would be the changes in particular?

There will be some adjustment of national law needed following the due incorporation of the Mortgage Credit Directive into the EEA legal order and consequent adoption by the Icelandic Parliament at national level. At this point in time, it is unclear whether there will be a separate law regulating this field – as recommended by Committee nominated by the Prime Minister.[42] According to the Committee changes would probably be necessary/advisable regarding the following:[43] authorisation and registration of credit intermediaries (European passport regime) allowed to offer mortgage credit; the authorisation, registration and supervision of other non-credit institutions offering mortgage credit; the limits of credit calculated on the basis of the commercial/official value of the property (maximum 80%); special rules on early repayment of the credit and the cost thereof; adaptation of tax regime and administrative fees for registration of mortgages; surveillance and enforcement of the law with appropriate administrative measures or sanctions for non-compliance with consumer mortgage law (similar to punitive damages currently possible under national competition law); creation of an Ombudsman for consumers, and revision of out-of-court redress bodies for the resolution of disputes between creditors and consumers and between credit intermediaries and consumers.[44] The Committee also advises limiting the guarantee which can be executed on the property if the borrower defaults, without a personal guarantee given on the present and future patrimony of the households (devolution of collateral cancels all remaining debt as in the American system) and introducing rules prohibiting the requirement of additional guarantees from third parties which have led to many cases of litigation before the courts and has complicated the process of debt-mitigation.

Further changes are unclear since Icelandic consumer and mortgage loans have been traditionally linked to the consumer price index calculated on the basis of inflation (CPI-indexed). The European Commission and EFTA Surveillance Authority (ESA) diverge on the legality of this practice and on whether or not price-indexation (which increases the *de facto* cost of credit) falls into the scope of the CCD as cost of credit or not. In a letter to the rapporteur MEMP, the Commission states that price-indexation is cost of credit, so it has to be calculated under the formula of annual effective rate of charge (APRC) and does not escape control of abuse under Directive 93/13 applicable to mortgage contracts. In contrast, the ESA holds the opinion that price-indexation is not cost of credit but an additional charge for credit currently falling outside the scope of the CCD. Whatever may be the case, both institutions agree that transparency and clarity of language for consumers is key. The Icelandic legislator as well as the Committee on Consumer Protection on Financial Markets have expressed their concerns about the potential illegality of the CPI-indexation practice (as it has been traditionally constructed) under EU law but have decided that the competence to clarify the legality of the question falls upon the national courts (and eventually on the EFTA Court through the advisory opinion procedure similar to the EU preliminary ruling question). Two cases are pending before the EFTA Court.

4. How is the national framework with regard to the UCT 93/13?

The UCT 93/13 was incorporated into domestic legal order by amendment to Article 36 of Act No. 7/1936 on contracts, agency and void legal instruments (through the EEA Agreement). It allows national judges to examine the legality and fairness of contracts in the light of circumstances taking place after its signature and entry into force and declare partial/total invalidity of those provisions.[45]

42 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 83-88.

43 *Ibid*, 2013, 83-88.

44 *Ibid*, 2013, 86 which mentions a similar conclusion by the Financial Supervisory Authority FME, Report on consumer protection in financial markets, 2011.

45 This has been criticised by the report of the Committee on Consumer Protection in financial markets (2013, 52) stating

Ása Ólafsdóttir, lecturer at the University of Iceland, who is currently doing research on the implementation of the UCT 93/13, provisionally concluded that Icelandic judges and lawyers think that traditional and older national contract law (Article 36 Act on contract law 7/1936 similar to other provisions in Scandinavian law) is more comprehensive than the "new" European law (Article 36 a-d) and valid also for small business, not only consumers. Article 36 has very rarely been applied by Icelandic courts in connection with consumer (credit) and mortgage issues. On the occasion of the accession negotiations, Iceland has recognised that full implementation of the Directive 93/13/EC is still needed:[46] Article 7 of the Directive is still unimplemented and no public institution exercises supervision over abusive clauses.[47]

V. Enforcement of consumer credit contracts

1. What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?

The rights and obligations of lender and borrower in case of default on monthly mortgage instalments are typically standardised. The most common legal consequences in case of default are:

- The borrower has to pay penal interest (Act on Interest and Indexation no. 38/2001).
- The lender can terminate the loan and demand forced sale of the mortgaged property without a verdict, court settlement, or attachment if certain conditions are met by the lender (Act on Contractual Mortgages no. 75/1997).
- If the loan is not fully paid despite the sale of the property the lender can demand full payment of the remaining balance of the loan as well as an attachment in other properties of the borrower without a verdict or court settlement (Act on Attachment no. 90/1989)

The lender and borrower's main rights and obligations are typically:

- The lender must receive due payment of amortization, interest, and all costs agreed upon in the loan agreement on due date.
- The lender can terminate a loan if the borrower defaults on the payment of interests and if amortization has been substantially delayed (Act on contractual Mortgage no. 75/1997, Article 9 (1) lit. a.)
- He must send the borrower in time before due date the instalment bill for the period which can be paid in any bank or make other arrangements for the borrower to be able to pay in due date.

2. What are the requirements to initiate enforcement procedures against the consumer?

The main requirement is that the borrower has not carried out full payment on the date it is due or that the guarantor seeks composition or their estates are declared for bankruptcy. The lender can also initiate enforcement procedures if, for example, the market value of the mortgaged property diminishes or if other creditors make a demand for the forced sale of the mortgaged property.

3. What are the steps of such enforcement procedure?

As a forced auction is most common when it comes to mortgage loans, the procedure described here relates to those agreements. A collection letter is sent to the borrower before the loan is terminated. A

(Contd.)

that the new legislation lacks a provision which had previously been included which sanctioned with partial nullity the failure of disclosure information on the part of the creditor. This detail could be of importance with regard to the disclosure of, for example, the effects of future inflation on the contract through the price-indexation clause. This issue will be elaborated on in section XI (behaviour of relevant actors).

46 Ministry of Foreign Affairs, Report on Chapter 28, 2012, 1-2 at www.eu.mfa.is.

47 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 58, 88.

written payment appeal is sent, advising the borrower to pay the due payment with penal interest, cost and collection cost within a certain timeframe (between one and four weeks). The collection letter informs of the consequences if this is not done, i.e. termination of the loan and enforcement procedure. Payment appeal is sent if the collection letter is not attended to. The borrower has fifteen days to react.[48] An auction request is sent to the proper District Commissioner if the payment appeal is not attended to. The District Commissioner examines whether the request meets legal requirements in the Acts no. 90/1991 to schedule a hearing. If at the auction an offer is made and all those requesting auction declare that they do not wish to hear any further offers the auction is considered complete, Article 34 Paragraph 2.[49] If the auction is not complete, a second auction will be held within four weeks.

4. Can the consumer raise substantive objections against enforcement?

a. Which ones?

In principle the consumer cannot raise substantive objections against enforcement. According to Article 22 (2) of Act no. 90/1991 on Forced Sale, objections from the consumer shall as a main rule not stop an auction unless the objections are of the nature which the Commissioner was obliged to examine himself[50] or if the Commissioner considers it otherwise uncertain that the lender has the right to demand an auction. The borrower could only stop the auction if he could provide substantial evidence that the claim had been fully paid at the time of the auction. As a reason it is pointed at the borrower's right to object the legality of the lender's claim after the sale according to chapter XIV of Act 90/1991, including the right to claim compensation if the claim was not legitimate. Hence, borrowers cannot claim at the (late) auction stage that contractual provisions and the lender's execution claim are invalid. It is not regarded as "substantial" at this point this point in time.[51]

Thus, the situation in Iceland is similar to the one in Spain (see the *Aziz* case). Ása Ólafsdóttir concludes that registrars and officials who oversee the enforcement procedure do not have the competence to stop the procedure or request a substantive assessment of abusive clauses detrimental to the consumer. Their role is to verify that formal requirements are complied with.

b. What is the legal effect of such objections?

The Commissioner can stop an auction if it is uncertain that the lender has the right to demand an auction. The borrower can seek a verdict in substance from the District Court. All further actions regarding the auction are stopped under Article 22 (3). According to chapter XIV of Act 90/1991, after the final sale the borrower can, by written request within 4 weeks, seek the solution of the District Court of the validity of the auction.

5. Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?

Yes, to a certain degree. Neither the Act on Forced Sale No. 90/1991 nor the Act on Contracts no. 7/1936 allow for adjustments of contractual terms in the case of "unforeseen/unforeseeable events". However, Article 36 of Act No. 7/1936 deems contracts void, partly or as a whole, and allow judges to

48 Act no. 90/1991 on Forced Sale, Article 9 and Act no. 19/1991 on Attachment, Article 7.

49 Act no. 90/1991 on Forced Sale, Article 34 Paragraph 2.

50 Those objections concern formal conditions such as the obligation of the Commissioner to send a registered letter to the borrower about the sale, the sale was advertised with all required information and in time, Articles 16, 19 and 20 and also if the auction request was sent to a Commissioner in another district than should have been, Article 13, Paragraph 2.

51 In the case Z-2/2013 an Icelandic District Court ruled that a legal proceeding could not be carried to conclusion within the framework of the legislation regarding enforcement without the creditor's consent. This then only leaves the option to oppose a claim on substantial grounds after the proceedings have been concluded by the district commissioner. This case has been appealed to the highest court. The consent of the creditor therefore seems essential and the debtor, alone, cannot oppose the enforcement procedure alleging a violation of European/national consumer law.

adjust them if they are considered unfair or against good business practice to uphold them. According to Article 36c a contract is unfair if it is not in compliance with good business practices and if it substantially disturbs the status of obligations and rights of the contracting parties to the detriment of the consumer. These terms have not been applied by the Icelandic courts to adjust contractual terms in consumer mortgage agreements despite claims that FX- and CPI- indexed loans are of such nature that their terms could be deemed void, given the multiplication of loan payments of the loans due to exchange-rate fluctuation and inflation.

In general, lecturer Ása Ólafsdóttir notes that the Supreme Court has been reluctant to follow this path after the financial crisis (the difficulty being the decision as to who bears the burden of proving the change of circumstances). Instead it has followed a formal assessment of whether all due legal requirements were respected or not. The change of circumstances approach was tried after the financial crisis, however this approach proved unsuccessful.[52]

a. How is the term "unforeseen/unforeseeable events" defined?

The term is not defined in legislation and left to judicial case-by-case interpretation. In general Icelandic law is not alien to the concept of "force majeure" whereas circumstances beyond parties' control (wars, earthquakes, civil unrest, etc) make it impossible the compliance with contract obligations on a temporary or permanent basis. The concept of force majeure does not generally apply to the financial crisis.

b. If adjustment is possible, what are its legal effects?

Adjustment of contractual terms through judicial decision is legally binding for both parties.

6. Does the applicable law allow for an adjustment of contractual terms in case of frustration of contract/purpose?

No.

7. Do the banks use private companies that deal with the recovery of debts with the result that legislation on consumer protection doesn't apply anymore?

In general the three main commercial banks re-established after the financial crisis deal with credit/mortgage loans of their customers together with the general provision of banking and financial services. Moreover, other financial institutions specialised in credit (ie. Lýsing) should not fall outside of the scope of the Act no. 1/1994 and 13/2013 on consumer/mortgage credit. However, there have been complaints about the enforcement of the car leasing/car loans through private companies because consumers had waved their rights (allowing companies to take repossession of the cars without the usual judicial procedure for the enforcement of contractual/property claims). The Supreme Court has ruled that this waiver of mandatory rights is invalid and, subsequently, legislation was amended to curb this practice.[53]

VI. National legal framework applicable for over-indebtedness

1. What are the possibilities for consumers in case they are considered "over-indebted"?

52 Ása Ólafsdóttir. Réttaráhrif brostinna forsenda í samningarétt, Háskóli Íslands, Þjóðarspegill 2012, at

http://skemman.is/is/stream/get/1946/13334/31994/1/Asta_Olafsdottir_Brotnar_forsendur_i_samningaretti.pdf

53 Many complaints have resulted from the resolution of the former saving bank SPRON and its company FRJÁLSI (ie. Drómi) because it was done through a company created ex novo to wind up the former state of the bank and maximize the assets of the bankruptcy state. This deprived consumers from the general application of consumer law as it was bankruptcy law which prevailed for most procedural questions. In January 2014 the loan portfolio of Drómi was bought by a commercial bank so substantive and procedural consumer law should apply.

Many temporary and a smaller number of permanent legislative measures in the immediate aftermath of the financial crisis were concerned with different strategies to mitigate debt for indebted consumers.

In general, Iceland followed a hybrid way of debt reorganisation and debt relief instead of a reduction of the principal owed. It relied both on encouraging direct collaboration between creditors and debtors to reorganise and re-structure debt (voluntary additional measures of debt-relief) and later providing a framework with limited general and conditional support measures for debt-mitigation (Debtor's Ombudsman). Only at a later stage the so-called 110%-way and special rebates were added (see below).

a. Is there the possibility for the consumer to reorganise debt or obtain debt relief?

Yes. re-organisation and (partial) debt relief were the objectives of both permanent and temporary measures within debt mitigation, (partial) payment freezing and smoothing, adopted since 2009. Debt relief continues to be an issue in Iceland.[54] According to the Act on Specific Debt Restructuring and the Act on Debt Mitigation discharge of debt is possible if payments according to a debt restructuring or mitigation contract are paid for three years. Individuals can also attain discharge of debt according to Act on bankruptcy No. 21/1991, chapter three (composition). A composition agreement may provide for total relinquishment of debts, proportional relinquishment, deferred dates of payment, changes in form of payment, or the three last mentioned arrangements jointly. Certain types of claims are excluded according to Article 28 (mortgage claims are amongst them), unless a creditor agrees with the applicability of the composition agreement concerning those claims. But generally, consumers cannot obtain discharge of debt arising from a mortgage agreement. Special debt relief (110%-way) adopted in 2011 allowed mortgage loan adjustments to 110% of the market value.

- Re-calculation of loans.

Probably the most important way for consumers to obtain partial debt relief has been the re-calculation of loans. Following the litigation that deemed FX-denominated loans illegal, re-calculation of such loans took place. Act No. 151/2010 concerning the recalculation of individuals' FX-linked mortgages and motor vehicle loans was adopted by the Parliament. Subsequently, banks have so far recalculated a total of 68,348 loans, 14,179 of them foreign-denominated mortgages, 45,668 foreign- denominated motor vehicle loans, and 8,501 ISK-denominated portions of mixed loans.[55] Details below.

- Debt Mitigation for individuals, Act on Debt Mitigation for individuals no. 101/2010.

The objective of debt mitigation is to enable individuals in "serious financial difficulties" to restructure their finances and bring balance between debts and debt service to make it possible for a debtor to meet his obligations for the foreseeable future. The individual seeking debt mitigation has to demonstrate that he cannot, or will in the foreseeable future not be unable to, repay maturing financial obligations, taking into account the nature of the debts, his assets and otherwise his financial and social circumstances. Debt mitigation may provide for: full relief of individual claims, the relative decline of individual claims, deferred payment of individual claims, changes of agreement terms, payment of individual claims by sharing the instalment amount to be paid at certain intervals during a certain period, modified form of payments of claims, or all of the above. 2,736 individuals had been through this measure at the end of 2012.[56]

54 IMF, World economic outlook: Growth resuming, dangers remain, Chapter 3. Dealing with household debt, April 2012, 89-124.

55 Central Bank of Iceland, WP 59, 2012, p27.

56 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24. See:

http://www.velferdarraduneyti.is/media/Rit_2013/Greinargerd-um-fjarhagsstodu-heimilanna_april2013.pdf

- Temporary Mitigation of real estate mortgage loans for homes, Act on temporary residential Mortgage Debt Mitigation No. 50/2009.

The owner of a residential property can apply for debt mitigation for the mortgage debts, if they demonstrate that they are and will for a period of time be unable to pay in full their financial obligations which are insured with a mortgage in that property, and that other debt restructuring measures are insufficient. Temporary mitigation can be maintained for up to five years. The obligations of the borrower change in the way that only payments which they are deemed able to cover are repayable on demand. The maturity date of the remaining financial obligations is postponed as long as the debt mitigation is in effect. 176 individuals had made use of this possibility by the end of 2012.[57]

- Temporary solution for individuals owning two homes/real estate, Act no. 103/2010.

Individuals owning two properties, one older and one newer intended as a residence for the family, can ask the mortgagee to overtake one of the properties on market value as consideration as full payment of the mortgage. 101 individuals had been through this measure at the end of 2012.[58]

Moreover, consumers had the possibility of making use of the following temporary measures:

- Freezing of payments, refinancing and longer maturities of loans

Households were able to freeze payments on FX-loans, because of the rapid depreciation of the domestic currency and the instability of the foreign exchange market in the immediate aftermath of the collapse of the Icelandic banking sector. This is not an actual debt restructuring measure but a forbearance measure designed to allow households to reassess their financial position. Borrowers could also freeze payments of other loans, refinance defaults of payments by adding the default amount to the principal or by issuing a new bond or have the maturity of loans prolonged. This was done in accordance with an agreement between the government, Icelandic Financial Services Association, the Housing Financing Fund, Icelandic Pension Funds Association and the bankruptcy estate of the savings fund SPRON (Drómi), dated 3 April 2009.[59] 3,056 individuals had been through these measures until the end of 2012.[60]

- Payment smoothing of CPI-indexed mortgages (Greiðslujöfnun fasteignaveðlána) (Act no. 133/2008).

The aim of this measure was to equalise the payment burden of CPI- indexed mortgage loans of individuals. Payment smoothing involves postponement of the difference between the payments according to the payment smoothing index[61] and the payments according to the consumer price index (CPI) until the payment smoothing index increases and becomes higher than the CPI. The difference was put into a special equalisation account, which is added to the principal value of the loan. If there was a debt on the equalisation account at the end of the maturity of the loan, the maturity is prolonged for three years. If there is still a debt on the account after that time the debt is cancelled. Only those who informed that they did not want this measure were excluded. After 2008 there has been room to

57 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24

58 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24.

59 See: http://www.ll.is/files/bcdihgggje/Samkomulag_um_greidsluerfidleikaurradi.pdf

60 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24.

61 The payment smooting index weighs together the wage index and employment condition. This means that if unemployment increases and other variables remain the same, both payment smoothing index and debt payments decrease.

allow debt smoothening, as between 2008 and May 2012, the CPI rose by 41%, while the payment-smoothing index rose by 24%. 21,241 individuals had gone through this measure at the end of 2012.[62]

- Specific Debt Restructuring – Act No. 107/2009 (Act on actions for individuals, homes and companies because of the financial crisis, expired 31 December 2012).[63]

The purpose of this legislation was to accelerate the restructuring of the Icelandic economy in the wake of the bank and currency collapse in the autumn of 2008 and to re-establish balance in the value of assets and payment ability on one hand and financial obligations of individuals, companies and homes on the other hand. Consumers could benefit from the measures contained therein if milder measures (such as freezing of payments and longer payment period) failed to achieve a permanent solution to financial difficulties. The requirements were that family income was sufficient to pay mortgage loans of distressed real estate which corresponds to 100% of the market value of property and a car.

If payment ability was less than 100%, specific debt adjustment provided the flexibility to switch to a cheaper property. In case of lower payment ability than of a loan corresponding to 100% of market value of the property, the payments could be based on 70% of the market value and a loan with no payments for three years on the second mortgage was provided for the residual 30%, which meant that the property was mortgaged for 100% of the market value, although payment ability was only for a 70% loan. Furthermore, it was expected that the borrower would sell other assets and only retain the residential property and a modest family car.

- 110% way – Adjustment of residential mortgages to 110% of the market value of the property, Agreement among lenders[64] on the real estate market in favour of over-indebted homes dated 15 January 2011.

Debts exceeding 110% of the market value of a residential property were written off. Where the borrower did have other assets[65] the write-off was adjusted in accordance with the value of the other assets. The Housing Financing Fund, the Pension Funds, Savings banks and Drómi followed the agreement as was, while the three big banks adopted another, often more favourable method. For example, they used a real estate evaluation instead of the market value, did not adjust the write-off in case of owning other assets (if the write-off was within a certain amount), etc. This led to different outcomes for borrowers with similar debts and assets, owing different lenders.[66] Of 15,137 respective

62 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24.

63 Greinargerð um fjárhagsstöðu heimilanna, April 2012, p. 24.

64 See: http://www.ll.is/files/bcdihgggje/Samkomulag_um_greidsluerfidleikaurradi.pdf

65 For example vehicles, summer houses, bank accounts etc.

66 Skýrsla eftirlitsnefndar samkvæmt lögum nr. 107/2009, September 2011, page 25.
See: http://www.atvinnuvegaraduneyti.is/media/Acrobat/Eftirlitsnefnd_.pdf

applications, 10,807 were accepted and 4,216 rejected.[67] The accepted applications also include cases where write-offs were adjusted due to other assets.

- Special interest rebate paid out in 2011 and 2012.

In addition to traditional interest relief a special interest subsidy was paid in 2011 and 2012 amounting to 0.6% of the debt due concerning property for residential use. The subsidy could not exceed ISK 200,000 for an individual and ISK 300,000 for married couples, single parents, or cohabiting partners for each year. The subsidy could not exceed the interest actually paid for the purchase or construction of private housing.

i) How are the terms re-organisation and debt relief defined?

In the Act on Debt Mitigation for individuals No. 101/2010, Article 1 (1) debt mitigation is defined as reorganisation of the finances of individuals in substantial payment difficulties in order to establish a "balance between debts and payment ability in a way which is realistic for the borrower to be able to meet his financial obligations in the foreseeable future." A definition of "debt relief" can be found in the Act on specific debt restructuring No. 107/2009, which expired on 31 December 2012. The definition refers to a contract between borrowers and lenders on debt relief or on restructuring the terms of bonds and loan agreements with the main objective to adjust debts to the payment ability and asset position of the individual or home in question.

ii) What are the requirements for re-organisation and relief?

Individuals seeking debt mitigation have to demonstrate that they cannot, or will be unable in the foreseeable future, to repay the maturing financial obligations, taking into account the nature of the debts, their assets and otherwise their financial and social circumstances.[68] In case of specific debt restructuring and debt mitigation, all lenders have to accept the agreement.

iii) How many consumers have had debt re-organised?

The data on this issue is not coherent. According to Central Bank data from 2012, 4,000 individuals applied for services of mediation under the Debtor's Ombudsman, and 1,300 for debt-reorganisation to banks.[69] The Ministry of Welfare provides data according to which 54% of loans are being restructured.[70] 21,241 debtors have benefited from debt-smoothing measures (House Financing Fund) and 3,056 have benefited from freezing payments to the commercial banks.[71]

iv) How many consumers have obtained debt relief?

The data on this issue is not coherent. According to the previous table, 824 and 2,736 debtors have benefited from special debt re-organisation procedures and 11,737 benefited from the 110% way. According to the association of financial institutions SFF, all in all, 83,677 households obtained some form of debt relief (data refers to 12 March 2012), of which 12,590 did so through the 110 per cent-way, 884 through special debt relief/restructuring, 12,984 through the re-calculation of loans, 4,610 through freezing of payments.

67 kýrsla eftirlitsnefndar samkvæmt lögum nr. 107/2009, December 2012, page 87. See: http://www.atvinnuvegaraduneyti.is/media/Skyrslur/Eftirlitsnefnd_skuldaadlogun_fyrirtaekjaskyrsla.pdf

68 Act on Debt Mitigation for individuals no. 101/2010.

69 Central Bank Report WP 59, p61.

70 Ministry of Welfare "Greinargerð um fjárhagsstöðu heimilanna", April 2013, p17.

71 Ministry of Welfare "Greinargerð um fjárhagsstöðu heimilanna", April 2013, p24.

In terms of amounts, Icelandic households had a total of 196.3 billion ISK (about 1 billion GBP) written off in relation to their debts[72] This amounts to about 12% of GDP. Financial institutions (SFF) provide similar numbers of 202.2 billion ISK. The write-offs consisted of:

- 3.6 billion ISK due to the adjustment of residential mortgages to 110% of market value.
- 6.2 billion ISK for other debt relief provided for households in "serious" difficulties.
- 108 billion ISK for recalculation of illegal FX-indexed mortgage loans (see below).
- 38.5 billion ISK for recalculation of illegal exchange-rate-linked car loans (see below).

b. What are the requirements for initiating bankruptcy proceedings for consumers?

According to the Act on Bankruptcy No. 91/1991, Article 64, a borrower can file for bankruptcy if they cannot pay in full his debts when they are due and if it is not considered likely that these financial difficulties will pass within a short time. The borrower has to guarantee the cost deriving from the claim of bankruptcy in case the cost cannot be paid from the bankruptcy estate, Article 67 (2). The fee is ISK 250,000, which many borrowers are not able to provide. The Parliament has changed in 2014 the legislation in order to facilitate bankruptcy procedures for individuals and to provide them with the fee necessary to file for bankruptcy.

With Act No. 23/2009 the Act on Bankruptcy was changed in favour of over-indebted individuals. The main changes were that claims asserted in the bankruptcy proceedings are prescribed (German: *Verjährung*) years years after the termination of the bankruptcy proceedings. Previously, this period was regularly four years with some claims prescribing after ten to 20 years depending on their nature. Another significant change was that the limitation period can only be interrupted through declaratory judgments. Such declaratory judgments will only be rendered if the creditor can demonstrate a special interest in interrupting the limitation period once more, and if it is likely that enforcement of the claim can be obtained in the new limitation period. These changes were made with a view to facilitating the possibility for individuals to declare bankruptcy in cases when financial institutions were reluctant to negotiate debt restructuring.

The change in the limitation period and the increased difficulties for the creditor to obtain a judgement to interrupt the limitation period, are supposed to help over-indebted borrowers to regain their financial status without being “hunted down” by creditors. However, as stated above in question II.5.b., “unsuccessful executions” have replaced bankruptcy proceedings and thus circumvent the protective goals of the new legislation. This is probably due to the fact that consumers are not completely aware of their rights and different procedures (as they can prevent this by filing for bankruptcy). Additionally, for those who are well-informed another obstacle appears: a bankruptcy procedure fee amount to ISK 250.000 which many cannot pay. From 2014 it will be possible to apply for financial legal aid regarding this fee under the supervision of the Debtors Ombudsman.

c. Is there a possibility for consumers to attain discharge of debt (Restschuldbefreiung) with bankruptcy proceedings?

Yes. The new Act on bankruptcy no. 2010/142 allows debtors a fresh start after two years. However, there is a sunset clause that allows the Parliament to re-evaluate the law after four years. Mortgage contracts can be enforced but a new rule of reimbursement of claims following forced sale after eviction has been adopted. The Debtor’s Ombudsman had received by mid-February 2014 a total of 59 grant application for financial support to initiate bankruptcy proceedings under the new law which is estimated to go beyond 100.[73]

72 Reply from Minister of Work and Innovation to the question of MP Einars K. Guðfinnssonar at http://www.althingi.is/altext/141/s/pdf/0575.pdf

73 New Act 7/2014.

i) How is discharge defined in the national context? (Is there a definition?)

One definition of discharge is contained in the Act on Bankruptcy, Article 29, Paragraph 2: "...total relinquishment of debts, proportional relinquishment, deferred dates of payment, changes in form of payment, or the three last mentioned arrangements jointly."

ii) If discharge is possible, after how many months/years is it possible?

In case of specific debt restructuring the discharge is possible after three years. In case of debt mitigation the discharge is possible after one to three years, depending on the time period of the agreement. In case of bankruptcy the discharge is possible after two years after the proceedings have been finalised.

iii) If discharge is possible, what are the requirements for discharge?

In bankruptcy proceedings the formal requirements are (i) to provide cash collateral (fees) for the cost of the bankruptcy administrator and (ii) the debtors' inability to pay their debts when they fall due. See Articles 64 and 65 Act on bankruptcy. A creditor can petition for a declaration of the debtor's bankruptcy in some situations when it is clear that the debtor is incapable of honouring his financial obligations in full when they become due, or will become capable of doing so within a short period of time. A debtor may petition for a declaration of his bankruptcy if they are unable to honour their debts to their creditors in full when they become due, provided it is not deemed likely that his payment difficulties will be over within a short period of time. A debtor who is obliged to keep accounts has the duty of filing a petition for his bankruptcy. The debtor cannot file for bankruptcy in two cases.

- If his claim is adequately secured by a collateral or other similar security interest in the debtor's or a third party's property, or by a guarantee extended by a third party;
- If a third party offers payment of the claim, or, if the claim has not become due, if a third party offers to secure the claim in a manner deemed adequate. The final requirement for discharge is the completion of a specific judicial bankruptcy procedure. Part IV of Act No. 21/1991 on bankruptcy establishes that the bankruptcy process is commenced with a ruling of a court of law. For commencement of bankruptcy proceedings a separate legal person is formed, i.e. the bankruptcy estate of the debtor, which bears the name of the debtor and takes over all his financial rights and obligations, except as otherwise provided by law. To carry out the liquidation of the estate, the judge will appoint a trustee in bankruptcy, who shall be a practising legal professional.

Generally speaking, the bankruptcy process consists of the trustee collecting the assets and rights of the estate and liquidating them in accordance with the further rules of the Act. The creditor must however declare the claim to the trustee in bankruptcy within the time limit set, otherwise the claim will be cancelled with regards to the estate. A composition agreement with creditors can be also reached before and during bankruptcy proceedings.[74]

iv) How many consumers have benefitted from debt discharge?

No data available for bankruptcy proceedings.

a. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

There is no legal limit for the duration of bankruptcy proceedings. In practice judicial proceedings may take up to one year at first instance.

74 More info at

http://www.innanrikisraduneyti.is/media/Skyrslur/Special_Committees_report..pdf

b. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can take recourse to? Please list and elaborate on requirements, legal consequences, and numbers of consumers who have gone through the measures in question.

No.

2. Is there a national legal or policy framework for avoiding evictions?

In the aftermath of the financial crisis, different measures were taken to avoid evictions, at least temporarily. A moratorium was adopted. Subsequent amendments to existing legislation concerned (less and less easier) requirements for the postponement of auctions of property.

A temporary provision was added to the Act on Distress Sale no. 90/1991, which obliged the Commissioner to comply with a borrower's request to postpone auctions of a property until 31 October 2009. With Act no. 108/2009, a new temporary provision was added to the Act on Distress Sale, stating that the Commissioner should comply with a borrower's request to postpone an auction until 28 February 2010 if auction was requested. Stricter conditions were made for the auction to be postponed i.e. the borrower had to live/reside at the property in question, it had to be his registered domicile and the property had to be defined as a residence property determined by planning authorities. With Act no. 11/2010, which expired 31 October 2010, yet a new temporary provision was added to Act on Distress Sale. According to the same conditions as in Act no. 108/2009, the Commissioner should comply with a borrower's request to postpone auction up to three months. This provision was extended until 31 March 2011 with Act no. 129/2010. At the moment, there is a moratorium on evictions in place until 1 September 2014,[75] which leads to an interruption of evictions because of the legal uncertainty over some mortgages (see below).

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (i.e. debt relief)?

Yes. Article 87 of the Act on Bankruptcy No. 21/1991, amended by Act No. 60/2010, allows individuals going through bankruptcy proceedings to remain in housing or have certain items (for example cars) at their disposal for up to twelve months. Rent has to be paid for the use, in respect of the possession; the trustee in bankruptcy may require the posting of security for any damage to the possession. A similar change was made to Act on Distress Sale No. 90/1991, Article 28, which gives the individual the right to live in the property for up to twelve months from the time at which the Commissioner received a payment of the auction prize. Rent has to be paid, the monthly fee corresponding to the amount which the Commissioner finds an appropriate. Specific Debt Restructuring and Debt Mitigation both provide for the affected persons to stay in their homes while proceedings are/were ongoing.

The financial institutions have also made rental agreements with borrowers facing auction after agreement to hand over the over-mortgaged properties. The rent period has been variable but in the majority of the cases it is pursued to give the borrower enough time to find another residence.

b. Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

There is no such possibility after the property in question has fallen into the property of the creditor, there is only the possibility to stay in the home for a certain period of time after an auction or bankruptcy proceedings as stated in VI. 2 a).

75 Act 7/2014.

VII. The regulation of credit bureaus[76]

1. How many credit bureaus are there in the country?

The only credit bureau in Iceland with a working permit for processing of personal data issued by the Icelandic Data Protection Authority is Creditinfo-Lánstraust hf. Other companies such as Keldan.is offer some personal financial information but do not have a working permit as a credit bureau; it mainly offers information from the real estate registry, registry of vehicles, the National Registry (registry of residents), registry of shareholders, and the tax registry.

2. Are the credit bureaus public or private?

Creditinfo is private. Iceland does not have public credit bureaus.

3. How are credit bureaus compensated?

Creditinfo has registered users which pay a monthly fee for their subscription.

4. How do the credit bureaus collect data?

Creditinfo uses official and unofficial data. Official data relates to data published in the Icelandic Law and Ministerial Gazette concerning, for example, bankruptcies and auctions, as well as information from the State Commissioner's registry. Unofficial data is provided by the registered users, for example information on mortgages and loans for houses and other real estate. Creditinfo also offers its users access to credit reports of borrowers which contain information about the borrower's financial background with regard to indebtedness (for example if he is in debt or in bankruptcy).

5. In what way do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

The Icelandic Data Protection Office issues a new working permit for Creditinfo every year allowing the process of personal data according to the Act on the Protection of Privacy as regards the Processing of Personal Data (available at http://www.personuvernd.is/information-in-english/greinar/nr/438). The work permit is reviewed every year and its terms and conditions examined. Creditinfo also states that they operate within the European Union Directive (95/46/EC) on the handling and transmitting of personal information.

6. What data is collected by credit bureaus?

Creditinfo offers information retrieved through third parties such as encumbrances, real estate information, registry of vehicles, rulings from the Supreme Court, the National Registry and others. Information obtained from Creditinfo can include credit reports, information from financial reports, information about the insolvency of companies, media information and information analysed through a payment behaviour system. Financial reports provide information on the financial standing of companies.

7. Who are the users of credit bureaus?

The users are creditors, such as companies, banks, individuals and parts of the Icelandic government. As for the Icelandic government, for example the State Commissioner uses Creditinfo for gathering information about individuals and companies, such as who is on the board or is the owner of a company. This is public information, accessible through Creditinfo. Other parts of the Icelandic government might use Creditinfo but only for the same purpose.

76 The information provided in this section VII is largely based on information obtained from the Icelandic Ministry of Interior and information on the website www.creditinfo.is.

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country? Elaborate.

Yes. The Central Bank of Iceland states in a report from 2011 that real house prices (albeit deflated by the consumer-price-index, CPI) had been rising steeply (by about 120%) between 1997 and 2007, an increase of 8% per year on average, with the largest increase taking place in 2005 (by one quarter).[77] However, the housing bubble has particularly affected some parts of the country (metropolitan area of Reykjavik and Reykjanes peninsula) but not all areas.[78]

2. What is the relation between housing prices and over-indebtedness?

a. How have housing prices developed since 2000 (or later if earlier data not available)?

The Central Bank states that housing prices doubled between 2000 and 2008, with the highest increase after 2004 with banks competing among each other as well as with the state-owned House Financing Fund (HFF).[79] After the financial crisis in October 2008 the property market fell approximately 34% (figure adjusted after inflation). At its worst moment, more than 27% of households were left in negative equity (with mortgages higher than the value of their homes). The situation has improved lately, for mainly two reasons:

- Debt-readjustment measures and policy instruments adopted by authorities that reduced - at least temporarily - mortgage debt, and
- Re-calculation of illegal FX-indexed loans.

As a result, the Central Bank researchers state that nominal house prices are now back to where they were in 2004-05 and are forecast to rise by some 5% between 2013 and 2014.

The recovery of the real estate market may also be due to the monetary policy currently in force. There are capital controls that limit the investment opportunities available for local savers/investors and there is a policy favouring foreign investments in the real estate market. The Central Bank of Iceland gives incentives to investors bringing foreign currency into Iceland for at least five years if they buy real state property. Moreover, there is also a high demand for housing in the capital area, as construction has been very limited since 2008 and the renting market is small.

b. How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available?

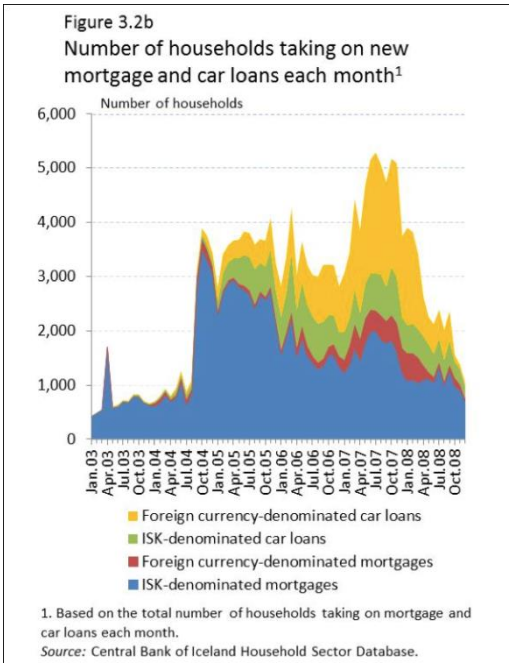
See answer to II.2.

Table 16 number of households taking new mortgage and car loans

77 Central Bank of Iceland, Monetary Bulletin 2001-2.

78 Ministry of Welfare, Status Report on the financial difficulties of households, June 2011, 7.

79 Central Bank Report WP 59, p71.



Source: Central Bank Report WP 59

3. *Has there been increased access to mortgage credit? In which way? For example: was access to consumer credit facilitated through legislation? Elaborate. And has access to credit become more restricted since the crisis? Elaborate. If possible provide data.*

There is evidence of a credit bubble in the years before the financial crisis. Both the Central Bank and Statistics Iceland have collected data that show the rising numbers of consumer indebtedness in those years (see also answers to questions 4 and 5).

Ása Ólafsdóttir, lecturer at the University of Iceland and doing research in consumer law, stated in an interview that the business model until 2008 was surely based on irresponsible lending practices when taking into account that 90% of the value of the loan was indexed to inflation (CPI) (in a country with a traditionally high inflation rate) and only 10% savings (assets) were required by the individuals.

The Central Bank states that creditors were expanding their lending activities to low-income and previously credit-constrained groups, distributing risk across the financial system through securitization.[80] Even though subprime lending was low (most of the debt was held by high-income households with low debt service burdens), there was a common over-estimation of the sustainability of the system in place: benevolent circumstances of rising housing prices, low inflation, stable exchange rates, and low interest rates.[81] The reference point in time for this expansion of credit is generally considered to be 2004, when the commercial banks were in direct competition with the state-owned Housing Fund HFF, which had eased its loan regulation to consolidate its position in the market. Better interest rates and easier access to mortgage credit meant more aggressive strategies for the acquisition of customers on the more competitive market. Especially FX- and CPI-indexed loans offered beneficial interest rates. The public House Financing Fund (HFF) never offered foreign currency loans or FX-indexed loans.

All of our interviewees mentioned a culture of over-spending in the boom years between 2000 and 2007 and easy access to credit. Business culture and practices encouraged consumers to put savings

80 Central Bank Report WP 59, p7.

81 Central Bank Report WP 59, p7.

into other financial products offered by banks (shares, investment funds). Moreover, over-consumption was fuelled by a practice of drawing equity from residential property.

Table 17: assets and liabilities of individuals, 1997-2012

Liabilities, assets and net worth of individuals by family type, age and residence, 1997-2012

	Total Assets	Real Estate	Vehicles	Other Assets	Total Liabilities	Mortgages	Other Liabilities
Total							
1997	881,904	588,351	76,958	47,839	339,001	224,331	114,670
1998	947,930	617,922	85,367	42,400	374,220	242,432	131,788
1999	1,083,954	722,130	96,543	43,340	424,712	281,339	143,373
2000	1,222,575	830,227	106,805	44,477	486,473	318,617	167,857
2001	1,395,411	979,333	104,772	49,687	561,649	373,274	188,375
2002	1,486,474	1,052,343	103,998	43,233	601,638	408,997	192,641
2003	1,676,563	1,194,650	108,576	45,172	678,606	460,380	218,226
2004	1,924,819	1,392,089	118,159	47,245	782,330	519,514	262,816
2005	2,508,965	1,861,400	142,012	49,670	948,850	612,257	336,593
2006	2,897,590	2,098,356	160,895	55,266	1,153,313	723,079	430,234
2007	3,471,164	2,440,535	188,239	62,458	1,399,810	861,993	537,818
2008	3,784,972	2,508,192	199,970	66,759	1,748,685	1,084,103	664,582
2009	3,877,349	2,585,562	190,425	65,889	1,999,613	1,195,410	804,204
2010	3,554,087	2,349,334	182,382	66,465	1,998,582	1,206,629	791,953
2011	3,736,345	2,581,048	180,842	69,587	1,886,177	1,182,811	703,366
2012	3,968,949	2,827,560	187,909	72,662	1,921,872	1,223,532	698,340

Latest update: 2014-02-07
Unit: Million ISK
Reference time: 1997-2012

Source: Statistics Iceland

Access to credit will surely be more difficult due to the new Act 33/2013 on consumer credit which tightens requirements (i.e.: checking information provided to the bank by potential debtor and testing credit history and real capacity of payment) and due to new Basil III rules which tightens international rules on leverage (expansion of banks' balance sheets in relation to own capital).

4. What is the relation between employment and over-indebtedness?

a. How many per cent of over-indebted consumers were fully employed / partially employed / self- employed / unemployed consumers at the point in time

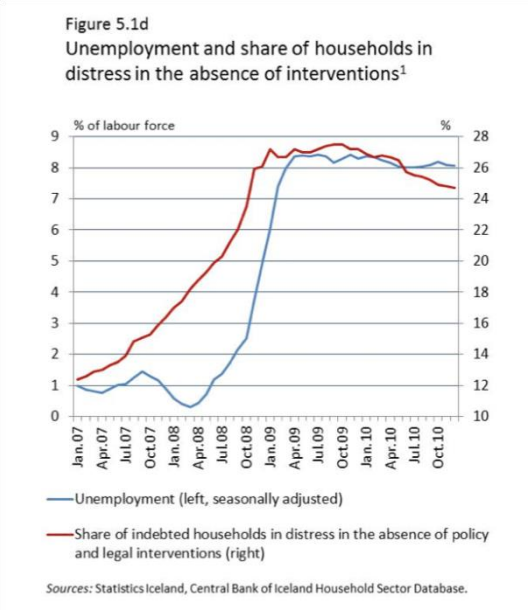
i) the credit contract was signed?

ii) when over-indebtedness arose?

There is no data on this issue. The Debtor's Ombudsman stated that since 2011 an average of 20% of those seeking assistance from the Debtor's Ombudsman were unemployed. In general, the unemployment rate in Iceland has seen an unprecedented increase in the direct aftermath of the financial crisis. Even though Iceland sees a relative low unemployment in comparison with other European countries, the extent of the sudden increase in unemployment after the financial crisis has to be taken into account. Moreover, unemployment might have been kept under control at a manageable level because of a loss of population due to emigration (from 2008 Iceland lost 8,692 individuals (net immigration) and rising student numbers registered at the Icelandic universities. The Central Bank Report WP 59 provides evidence that unemployment and levels of over-indebtedness correlate. The report furthermore notes that "both FX and ISK borrowers' capacity to withstand the rise in debt service was undermined as real wages declined … employment decreased, and unemployment rose …".[82]

Table 18: unemployment and households in distress

82 Central Bank Report WP 59, p. 72.



Source: Central Bank Report WP 59

b. How has the average salary evolved since 2000?

The nominal value of salaries has risen by more than 100% between 2000 and 2012 (from 210,000 to 474,000 ISK).[83] However, we have to consider that constant inflation of almost 300% within the last 20 years, and still almost 200% since the year 2000.[84]

5. Non-EURO countries: Did national monetary policy play a role in consumer credit and mortgage agreements?

It is now a commonly accepted view that the scale of the over-indebtedness problem is not only due to an expansion of credit but also to the nature and cost of credit which is indexed to inflation. This widespread practice is still considered legal and allows creditors to raise (ex post) the cost of credit.

a. Are/were foreign currency loans common?

Price-indexed and foreign-currency-indexed loans are and were the most important issue in the over-indebtedness of Icelandic consumers. In order to escape traditionally high interest rates in Iceland, consumers made extensive use of the following possibilities:

- loans taken in consumer-price-indexed ISK following inflation (CPI-indexed loans). Only loans offered to consumers by House Financing Fund (HFF) until 2004.
- foreign-denominated loans taken mostly in local currency (ISK) but indexed to foreign currencies following exchange rate variations (FX-indexed loans). Most widespread 2004-2008.
- foreign currency loans. Least common available since 2004[85]

According to the Central Bank[86] in 2008 there were 68,348 foreign-denominated loans, 14,179 of them foreign-denominated mortgages, 45,668 foreign-denominated motor vehicle loans, and 8,501 ISK-denominated portions of mixed loans (numbers calculated on the assumption that all foreign-

83 http://www.statice.is/Earnings+in+the+private+sector

84 Statistics Iceland. http://statice.is/Statistics/Prices-and-consumption/Consumer-price-index.

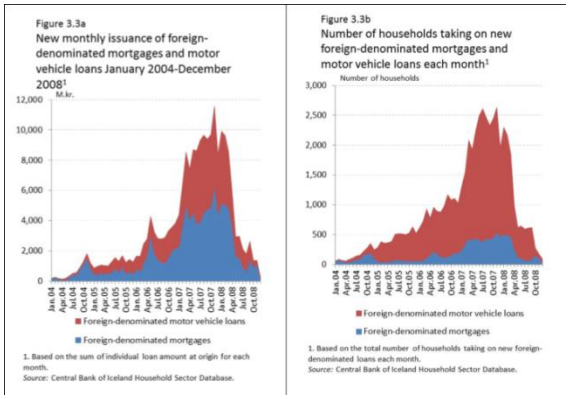
85 Some were offered to companies and/or individuals have been tested by litigation and declared legal (ie: those offered by Íslandsbanki have been declared legal by the Supreme Court on the basis of formal aspects but not material grounds).

86 WP 59, 2012, 29.

denominated and mixed loans were recalculated as of 31 August 2010). About a fifth of total household debt was foreign-denominated at the time of the banking collapse. Close to 84% of total outstanding motor vehicle debt was foreign-denominated at year-end 2008, as opposed to only 15% per cent of mortgage debt.[87] However, both increased significantly between 2004 and 2008.

87 Central Bank Report WP 59, p18.

Table 19 numbers of foreign-denominated loans 2004-2008



Source: Central Bank Report WP 59

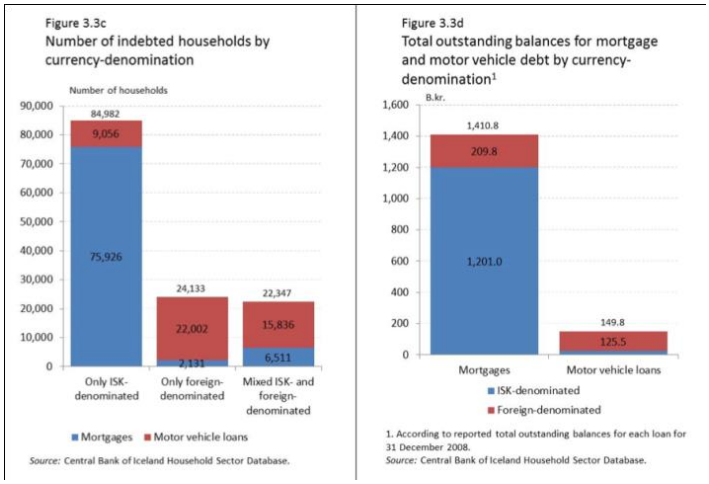
b. What are the foreign currencies in which loan agreements were concluded?

Foreign currencies used to contract foreign loans or to index ISK loans were usually euros, yen, Swiss Francs or a mix of different currencies. Exact data on the prevalence of the use of these currencies could not be found, but these were the most prominent.

c. Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?

Yes. The Central Bank reports that 23% of households with FX-indexed debt had monthly debt payments exceeding 40% of their disposable income, rising to 66% in 2009 and decreasing to almost 33% in 2010, taking into account the effect of the re-calculation of FX loans. The numbers for ISK-denominated debts only are much lower: from just above 7% in 2007 with a heavy debt burden, rising to 14% in 2009 and falling to 9% in 2010.[88]

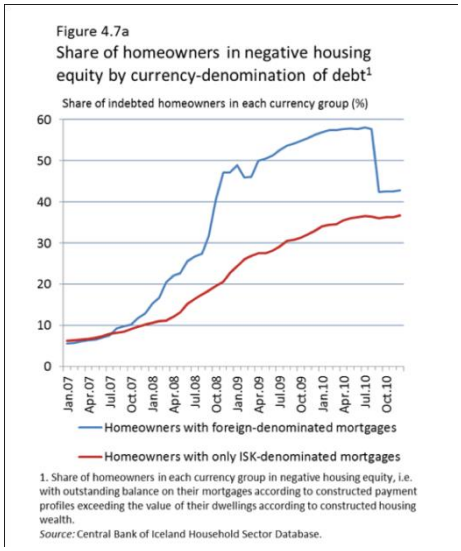
Table 20: number of indebted households by currency-denomination of debt



Source: Central Bank Report WP 59

88 Central Bank Report WP 59, pp41-42.

Table 21: share of homeowners in negative housing equity by currency-denomination of debt



Source: Central Bank Report WP 59

After the financial crisis, the principal sum borrowed on indexed loans rose either because of inflation (the relevant inflation index increased 37.5%) – in the case of CPI-indexed loans - and/or because of the devaluation of the local currency ISK by at least 50% against the Euro (the average exchange rate during 2007-2008 being around 1€= 85 ISK and since 2009 1€ = 160 ISK) – for foreign-currency and FX-indexed loans.[89] In 2010, almost a third (31%) of households with FX-indexed loans were facing serious financial difficulties. The share of homeowners with CPI-indexed loans and negative housing equity combined increased more than the share of homeowner with FX-indexed loans and negative housing equity combined.

The nominal outstanding amounts for FX-indexed loans nearly doubled due to the dramatic devaluation of the Icelandic currency in the autumn 2008. That situation changed when those loans were deemed illegal and were recalculated but still the share of FX borrowers in distress is roughly twice as high as that among ISK borrowers.[90] It is noteworthy that households in the second-highest quintile seem to have benefitted most from the recalculation of foreign-denominated loans (see below), as the share in distress declined by 4.3 percentage points afterwards. For comparison, the decline was 1.2 percentage points in the lowest quintile and 2.3 percentage points in the second-lowest quintile. This reflects that high-income households were more likely to have FX- denominated debt.[91]

6. *Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?*

The current main macro-economic risk factor is the finalisation of the restructuring process of the banking sector (still under resolution committees) and a clarification of legal issues still pending before the courts. Moreover, fragility of corporate and household position with high indebtedness in historical and international context (number of individuals on the default register has increased in the last months). Also, the revaluation of loans in the banks' portfolios on their reserves will be

89 Data from Central Bank and Statistics office. Exchange-rates reflect average values during the periods indicated.

90 Households' position in the financial crisis in Iceland, Working paper No. 59, Central Bank of Iceland, 2012, by Thorvardur Tjörvi Ólafsson and Karen Áslaug Vignisdóttir, p. 76.

91 Central Bank Report WP 59, p34, Figure 4.1c.

exacerbated in the future by the necessity of lifting current controls on capital movement and FX-operations. Finally, Iceland currently faces balance of payments difficulties in connection with non-residents' ISK positions.

IX. Micro-economic risk factors for over-indebtedness (consumer behaviour)

1. *What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)*

The most common consumer credit agreement concern housing and motor vehicles. When indebted households are categorised by the type of debt they hold, almost 84,600 households are mortgagors and 46,900 households have motor vehicle loans, while 34,900 households have both types of debt.[92] In the run-up to the crisis people were increasingly also taking new loans for mortgage equity withdrawals, often if not always to refinance older mortgage loans and to finance general consumption at the same time. Vehicle purchasing loans were very common before the crisis, as well as overdraft loans and credit card obligations (still common), financing general consumption and moveable property of all kinds (for example big flat screen TVs, which became a symbol of overconsumption in the wake of the crisis). Lease contracts were also made to purchase cars and other moveable property. Moreover, student loans are offered by the public institution LÍN (the Icelandic State itself does not provide grants for graduate or postgraduate studies). Even though they do not fall within the scope of this study due to the difficulties of compiling data on them, they add to the situation of over-indebtedness of households. Most consumers also have credit cards and use overdraft facilities.

2. *How many credit agreements do consumers conclude on average?*

The data provided so far in this study suggests that most consumers have mortgage and motor vehicles loans. All of the indebted households had mortgages, car loans or overdraft loans.

3. *Was/is the housing market in the country based on rent or ownership?*

The housing market is dominated by ownership. In the year 2009 the total of privately owned property was 99,965 or 77% of all residential property. Just over 85% of all Icelandic people lived in their own property in the year 2009.[93] Political initiatives in the second half of the 20th century, especially in terms of social housing, have not changed the fact that home ownership in Iceland remains one of the world's highest.[94]

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if data available)?*

According to data provided by the National Registry,[95] the number of mortgages rose continuously until 2007, from 5,809 in 1990 and 10,100 in 2000 to 15,252 in 2007. Ever since, the number of mortgages has decreased to 7,623 in 2012.

According to the Central Bank, the number of households concluding new mortgages peaked at the end of 2004, reaching almost 4,000 each month. The number shrank until October 2008, however

92 Central Bank Report WP 59, pp15-16, see also Table 4.

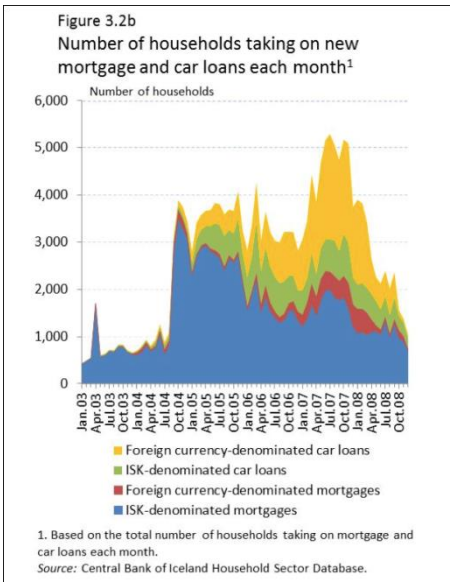
93 Skýrsla samráðshóps um húsnæðisstefnu 2011, page 21 and 22. See: http://www.velferdarraduneyti.is/media/frettir2011/19042011_Skyrsla_samradshops_um_husnaedisstefnu.pdf.

94 Sveinsson, "The Formation of Urban Homeownership in Iceland", Cambridge Conference Paper, available at https://borg.hi.is/The%20Formation%20of%20Urban%20Housing%20Policy%20in%20Iceland.pdf.

95 http://www.skra.is/library/Samnyttar-skrar-/Markadsfrettir/tafla2.1_2012.xls .

staying between 1,000 and 2,000 each month from 2006 to 2008 (the largest part of those mortgages was taken on as foreign currency-denominated loans).

Table 22: numbers of households taking on new mortgage and car loans 2003-2008



Source: Central Bank Report WP 59, 2012

5. *How many indebted and over-indebted consumers have credit card debt?*
   a. *How high is this debt?*
   b. *How long does it take consumers on average to repay credit card obligations?*

No public data is available on how high credit card debt is or how long it takes consumers on average to repay such obligations. However, these debts were very common and very difficult for the consumers in the wake of the crisis as, in the beginning, for example credit card companies did not participate in the Specific Debt Restructuring programmes. This has changed and now consumers can benefit from debt restructuring also with regard to credit card debt.

6. *How many per cent of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?*
   a. *How high is this debt?*
   b. *How long does it take consumers on average to repay overdraft facility debt?*

No public data is available specifically on how many per cent of consumers struggle with repayment of overdraft facility debt, or how long it takes to repay overdraft facility debts or overdraft facility obligations. However, these debts were and still are extremely common. They reduced rapidly in 2009 but increased again in 2010, see table below.

Table 23: overdraft debts of households

Source: http://data.is, Central Bank database.

In 2009 At least one bank, Íslandsbanki, offered customers the option to lower their overdraft steadily over a specific period against drops in interest on the overdraft. The requirement was that the overdraft was fully paid up within three years and overdraft debt did not exceed one million ISK.

7. *Is there a relation between the length of the credit obligation and over-indebtedness?*

    a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*

There is no data available on this issue. However, research by the Central Bank of Iceland has shown that debts arising out of motor vehicle loans, which in Iceland are usually short-term (usually less than ten years), play an important role in the over-indebtedness of households, due to high rates of debt-at-risk.[96] The Central Bank data also shows that the second highest debt-at-risk relate to overdraft debt, and the third highest to mortgage debt.[97] It is difficult though to establish a relation to the time period for which those debts were contracted.

    b. *How long are the time periods for which consumers took on credit and mortgage obligations? Is there a difference in data from before and after the crisis?*

There is no data available on this. Anecdotal evidence suggests that general consumer credit obligations are taken on for one to five years. The mortgage obligations are most often 25-40 years, in order to make the payments easier and/or to be able to buy more expensive properties. This was common practice of both the Housing Financing Fund and the Pension Funds on the one hand and the commercial banks on the other.

    c. *What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?*

No data available.

96 Central Bank Report WP 59, p76.

97 Central Bank Report WP 59, p78.

X. Relation between income and (over-)indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

Table 24: average household expenditure and size by disposable income, 2001-2012

Average household expenditure and size by disposable income fr om 2003

	Per cent									
	Total									
	2001-2003	2002-2004	2003-2005	2004-2006	2005-2007	2006-2008	2007-2009	2008-2010	2009-2011	2010-2012
01 Food and non-alcoholic beverages	15.2	14.4	12.9	12.8	11.8	12.9	13.9	14.1	14.7	14.9
02 Alcoholic beverages and tobacco	3.7	3.2	3.0	2.9	2.8	2.7	3.1	3.5	3.4	3.3
03 Clothing and footwear	5.5	5.2	4.8	4.7	4.9	5.0	5.5	5.7	5.4	5.0
04 Housing, water, electricity, gas and other fuels	22.5	22.9	25.4	25.6	25.7	25.9	24.7	25.1	26.5	27.0
041 Actual rentals for housing	2.3	2.2	2.0	2.1	2.2	2.6	2.8	3.4	4.1	5.2
042 Imputed rentals for housing	12.8	13.3	15.5	15.6	15.2	15.2	13.2	13.4	13.9	13.7
043 Regular maintenance	3.6	3.8	4.2	4.2	4.3	4.3	4.6	3.9	3.2	2.7
044 Other serv. relating to the dwelling	1.0	0.9	1.0	1.0	1.0	1.1	1.2	1.4	1.6	1.8
045 Electricity, gas and other fuels	2.8	2.6	2.7	2.7	3.0	2.7	2.9	3.0	3.7	3.6
05 Furnishing and household equipment	5.9	5.9	6.6	6.4	6.6	6.5	6.7	5.6	4.7	4.7

Yearly expenditure figures in this table are based on the household expenditure survey that has been a continous survey since the year 2000. The results are a three year average at price levels of the last year. Some COICOP classes have a standard error of mean larger than 20%. These classes are specified in the printed results of the household expenditure survey published in Statistical Series.

Latest update: 2013-12-13

Unit: ISK and per cent

Reference time: 2003-

Source: Statistics Iceland.

Different numbers are provided by Statistics Iceland in the Household Expenditure Report for 2012. Therein, it is stated that in 2011 on average Icelanders paid 18.1% of their disposable income on housing cost. That includes mortgage payments, interest and index cost, insurance, maintenance, electricity, heating and real estate taxes.[98] 11.3% of Icelanders spent over 40% of their disposable income on housing cost, which is considered to be overburden.

Table 25: share of housing cost in disposable income by tenure status

Tafla 1. Hlutfall húsnæðiskostnaðar af ráðstöfunartekjum eftir stöðu á fasteignamarkaði
Tafla 1. Share of housing cost in disposable income by tenure status

	Hlutfall *Rate*								2011	
									Vik-mörk *CI*	Áætlaður fjöldi *Esti-mated number*
	2004	2005	2006	2007	2008	2009	2010	2011		
Alls *Total*	**16,9**	**18,3**	**18,7**	**16,6**	**16,5**	**16,4**	**17,5**	**18,1**	**± 0,5**	**300.800**
Eigandi *Owner*	17,0	18,6	19,0	16,5	16,3	16,0	17,1	17,2	± 0,5	234.200
Eigandi, skuldlaust *Owner, no mortgage*	12,2	12,5	13,7	10,7	10,1	10,1	9,4	10,6	± 0,8	45.500
Eigandi, lán *Owner, with mortgage*	17,9	19,8	20,2	17,4	17,5	17,2	18,4	18,7	± 0,7	188.700
Leigjandi *Tenant*	16,4	17,0	16,8	18,1	19,5	20,1	19,8	22,3	± 1,5	66.500
Leigjandi, markaðsverð *Tenant, market price*	19,7	21,6	21,4	19,9	23,8	22,6	22,6	24,9	± 1,9	33.200
Leigjandi, lækkað verð *Tenant reduced price*	13,1	12,2	14,3	15,5	15,4	15,3	14,2	18,9	± 2,3	33.300

Skýringar *Notes*: Sjá mynd 1. *C.f. mynd 1.*

Source: Statics Iceland Household Expenditure Report 2012

98 Statistical Series, 2012:8, Disposable income and housing cost 2011. See: https://hagstofa.is/lisalib/getfile.aspx?ItemID=13864

Table 26: housing cost overburden by tenure status

Tafla 2. **Verulega íþyngjandi húsnæðiskostnaður eftir stöðu á fasteignamarkaði**
Tafla 2. *Housing cost overburden by tenure status*

	Hlutfall *Rate*								2011 Vik-mörk *CI*	2011 Áætlaður fjöldi *Esti-mated number*
	2004	2005	2006	2007	2008	2009	2010	2011		
Alls *Total*	**10,3**	**12,5**	**14,3**	**10,5**	**11,4**	**9,5**	**9,6**	**11,3**	**± 1,3**	**33.000**
Eigandi *Owner*	10,2	12,7	15,1	10,9	11,3	8,9	9,0	10,0	± 1,4	23.400
Eigandi, skuldlaust *Owner, no mortgage*	6,4	7,2	7,6	6,8	5,0	4,4	3,8	6,5	± 2,3	3.000
Eigandi, lán *Owner, with mortgage*	11,3	14,1	17,2	11,8	12,6	9,9	10,1	10,8	± 1,6	20.400
Leigjandi *Tenant*	10,6	10,8	8,4	7,8	11,5	12,6	12,6	16,4	± 3,4	9.600
Leigjandi, markaðsverð *Tenant, market price*	12,2	16,0	13,2	9,4	17,3	15,7	16,5	18,6	± 4,8	6.100
Leigjandi, lækkað verð *Tenant reduced price*	9,0	5,6	3,6	6,3	5,1	9,0	6,7	13,7	± 4,5	3.600

Heimild *Source*: Eurostat.

Source: Statics Iceland Household Expenditure Report 2012

According to the Central Bank of Iceland, approximately 74% of Icelandic households spent less than 30% of their disposable income on mortgage payments but around 12% had to spend over 50% of their disposable income in 2009. Around 63% of households with overdraft spent within 2% of their disposable income on respective interest payments. 7% of households spent over 10% of their income on interest payments. Approximately. 80% of households with car loans spent within 20% of their disposable income in payments. 11% of households had to spend over 30% of their income on car loan payments. Debt service on all debts was within 40% of disposable income of around 77% of households but one of every six households had to pay more than 50% of their disposable income on debt payments.

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

   a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate the risk through higher interest rates?*

No, they do not. In principle, there is no legal discrimination in Iceland based on income. But usually in mortgage agreements higher interests are paid with regard to the correlation between the percentage of the loan amount and the value of the mortgaged property. It is more likely that a low-income consumer has to mortgage his property more than a high-income consumer. Moreover, if debtors did not have a high income or many assets, there was a need for extra guarantees from third parties.

   b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

Concrete data not available, but see answer to X.2 lit a). Generally, low-income consumers are more likely to be struggling with loan payments and have higher loan obligations in relation to income. Households with the most heavy/burdening debt service are the households have a tendency to be in the lower-income groups.

   c. *Are there other key terms which change according to the income of the borrower?*

No data

Behaviour of actors in relevant cases

XI. Irresponsible lending practices

1. Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)

All, except one, consumers interviewed had contacted the bank for a mortgage loan, in part after having seen advertisements for loans. In general, the following observations shall be made. The banks and financial institutions advertised heavily in the years before the crisis. In 2004 public policy started promoting the purchase of houses, alongside banks, which started a massive advertising campaign introducing 90-100% LTV loans. A former bank salesman in one of three biggest commercial banks in Iceland, stated in an interview with one of the rapporteurs that in the years before the financial crisis the sales department was increasingly calling up customers and potential customers to offer them package products, such as savings and debit cards accounts and small loans according to their age. Many 16 to 20 years olds were offered prepaid credit and debit cards as well as arrangements for student loans; 20 to 25 years olds were offered overdraft facilities together with credit and debit cards; generally, people more than 18 years old were moreover offered pension and insurance agreements. Moreover, there was both a lot of advertising of housing loans as well as demand from consumers who had been called and asked for them.

2. Was a creditworthiness assessment undertaken before granting the credit?

a. In how many cases were creditworthiness assessments undertaken?

Creditworthiness assessments were undertaken, but not for all loans since it was not obligatory unless a third party issued a guarantee. Based on information through interviews, we assume that expenditure capacity assessment (*greiðslumat*) was usually done for debtors taking ISK-indexed loans from the House Financing Fund. The Association of Financial Institutions confirmed in an interview with one of the rapporteurs that the general culture of the banks merely asking "how much do you want?"

b. Who was the initiator of the creditworthiness assessment?

The loan departments of the banks.

c. Who undertook the creditworthiness assessment?

See b.

d. What were the criteria of the creditworthiness assessment?

No official data available. According to information given by a former bank salesman, a so-called expenditure assessment (*greiðslumat*) was undertaken, on the basis of income and payment obligations. The assessments included information on the size of the personal overdraft facilities, credit card statements, payment difficulties, and other information about assets/liabilities. Furthermore, a creditworthiness assessment concerning housing loans was said to require a tax statement, in which information beyond that was included, such as information on student and car loans, loans from pension funds or other assets.

For the first time, the criteria of the creditworthiness assessment are now defined in Article 5 lit. d) in the Act on Consumer Loans No. 33/2013.[99] The criteria is calculations of the payment ability of the borrower taking into account his assets, debts, expenses and income, which among other are based on official consumer guidelines. The Ministry of the Interior can issue regulations on the execution of

99 In Icelandic: d. Greiðslumat: Útreikningur á greiðslugetu lántaka miðað við eignir, skuldir, gjöld og tekjur, sem m.a. byggjast á opinberum neysluviðmiðum.

new tests: creditworthiness or credit history (*lánhæfismat*) and capacity to pay the loan (*greiðslumat*), but it has not done so as yet. The difference between a credit worthiness assessment and capacity to pay assessment is that the former is based on information of the business history of the borrower to try to establish how credible he is as a borrower and the probability of his ability to repay the loan. The latter is based on the actual calculations of the liquidity of the consumer of this particular loan, taken into account payment of other debts, taxes and assets and the cost of living.

e. Was a credit bureau involved?

The former bank salesman stated that the loan department sent inquiries concerning payment obligations etc. to Creditinfo-Lánstraust. A respective obligation is included in the new Act on Consumer Loans no. 33/2013.

3. Is there a legal obligation for a mandatory creditworthiness assessment? What are the criteria for creditworthiness assessment in legal provisions?

The Act on Property Issues no. 44/1998 in its Article 18 only required the Housing Financing Fund to undertake a creditworthiness rating assessment of the borrower before lending, but only when a third party provided additional personal guarantees over a mortgage loan. The practice was based on an agreement made by the government, the Consumers' Association of Iceland, and the Icelandic Financial Services Association.[100] It is impossible to know to what extent this obligation was observed in practice as credit could have granted despite a negative outcome of the assessment if other personal or extra guarantees were given (from assets from third persons (family) or other assets or income).

The new Act on consumers No. 33/2013, which came into effect on 1 November 2013, differentiates between "credit worthiness" and "capacity to pay the loan". According to Article 5 lit i) credit worthiness assessment is an assessment of the borrower's ability to repay according to information which is deemed likely to give reliable information of the probability of the borrower to honour his obligations under the loan agreement. Such an assessment, which is mandatory, has to be based on the financial history between the lender and borrower and/or information from credit bureaus. The double assessment is only necessary when specifically stipulated, i.e. in cases in which the loan is ISK 2 million or more for individuals or ISK 4 million or more for couples. See the criteria in lit d) below.

4. Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?

There is no data available concerning this question, except in some cases litigated before the Supreme Court (see litigation section). In two cases where the consumers won the case this assessment was wrong and the additional personal guarantee given by a third person was cancelled (cases nr. 4/2013 and 127/2013). In one case the guarantee from the third person was reduced as the assessment was partially wrong (case 169/2012).

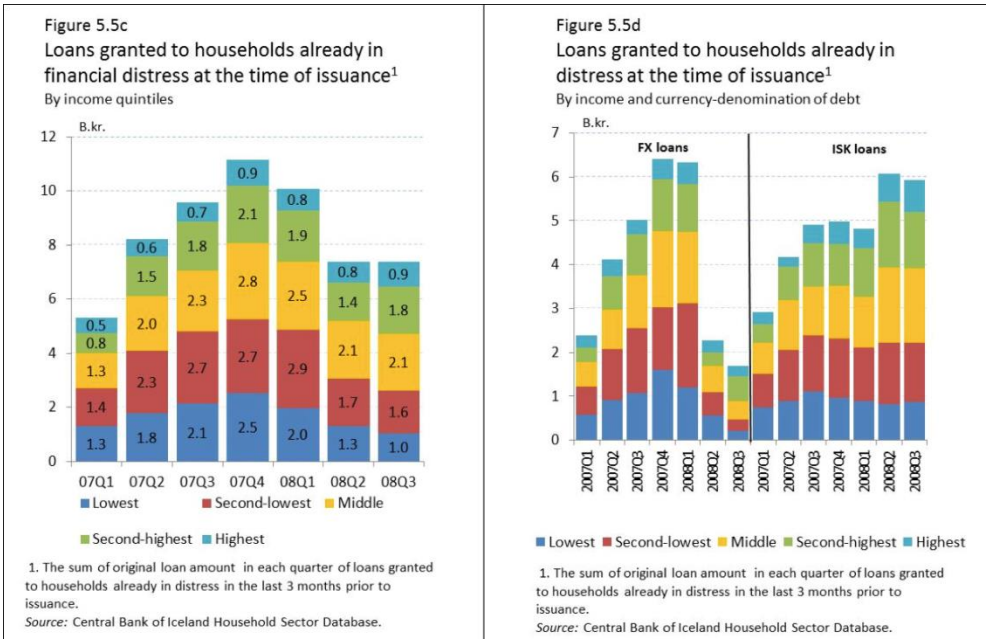
Irrespective of creditworthiness assessment, it should be borne in mind that in practice very often new loans were given to households already in distress – a practice which the Central Banks deems to have exacerbated over-indebtedness.

> "… In far too many instances, households already in distress were granted new loans that exacerbated their over-indebtedness and sent them deeper into distress. Prudent lending standards and screening activities by publicly- and privately-owned financial institutions should have prevented such a rapid build-up of vulnerability. Of course, this debt accumulation by distressed households also represents reckless borrowing on their part. However, financial institutions' main role is to serve as an efficient intermediary between savers and borrowers by screening and monitoring borrowers in order to ensure, to the extent possible, that only creditworthy households

100 Act no. 32/2009 on Guarantors came into effect in April 2009 and incorporates articles similar to the agreement.

and firms are granted loans."[101] And: "Some of the seeds of households'' financial difficulties were sown by imprudent lending in 2007 and 2008, when 16 per cent of the total amount of new loans was granted to households already in distress. Up to 34 per cent of households in distress at year- end 2010 were granted loans in 2007-2008, when they were already financially distressed. …"[102]

Table 27 - Irresponsible lending practices – loans granted to households already in financial distress



Source: Central Bank Report WP 59

This indicates the occurrence of 3 possibilities:

- creditworthiness assessment was not undertaken,
- the parameters for the creditworthiness assessment were not sufficient to realistically assess the financial capacity of households over a long time period where difficult problems might arise (loss of income due to external circumstances), or
- negative assessments were ignored.

5. *Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?*

All interviewed consumers answered this question in the negative. With the new Act on Consumer Loans no. 33/2013 this provision of information is mandatory.

6. *Did the consumer feel pressured by the lender, for example with regard to the signing of the contract, the amount borrowed, or in any other way?*

All interviewed consumers answered in the negative. Two consumers, however, elaborated that there was the understanding that it would have been no problem to get a higher loan, even though the consumer already took a higher loan than necessary, and that they felt like they were creating problems when asking for a payment plan.

101 Central Bank Report WP 59, p82.

102 Central Bank Report WP 59, Abstract.

XII. Irresponsible borrowing practices – emphasis on mortgage

As stated in the answer to question XI.4 the Central Bank Report WP 59 also acknowledges the responsibility of households in distress in situations when they took on new loans, for example. Generally, it can be said that the Icelandic society in the early 2000s was characterised by a wave of optimism, fuelled by economic growth, business expansion, high and rising salaries and easy access to credit. The authorities promoted the view that Iceland was a model of financial services success within the country and also abroad.

1. *Did the consumer read the agreement before signing?*

The majority of the interviewees stated that they had read the agreement (6/10). One reported problems with the Icelandic legal terminology and another one refrained from reading the contract after having been told that the contract was *"pro forma"*. In general, it is commonly known that loan agreements before the crisis were often done in haste.

2. *Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?*

Four consumers did compare different offers, while six did not.

3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*

While the consumer interviews showed that, in general, there was an opportunity to ask questions, the ones that did ask questions did not get satisfying answers.

4. *How much time did the consumer take before signing the agreement?*

According to the interviews, consumers took between very little and two to three weeks to sign the agreement.

5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

Before the Act on Consumer Loans No. 33/2013, which came into effect on 1 November 2013, consumers did not have any right of withdrawal except according to the Act on selling financial services through a phone No. 33/2005, the period being fourteen days, 30 in case of life insurance. The withdrawal period in Article 16 of new Act on Consumer Loans is fourteen days. We could not obtain any information on the use of that right in practice.

Litigation

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*

Yes. Litigation on the legality, content and execution of mortgage or car agreements has been very important in Iceland after the crisis, especially for households and companies with FX-indexed loans. There have also been cases concerning the validity of additional guarantees given by third parties (usually family members) on mortgages. Litigation on the legality of CPI- loans is pending.

   a. *What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law relevant in the adjudication – if yes, which ones?*

Applicable law was mostly national contract law and constitutional law with some indirect influence from the European Convention of Human Rights (Article 1). Although in several instances cases lawyers, individuals, companies, public authorities (talsmaður neytenda – the Consumers' "spokesman") and consumer associations tried to emphasise the effect of EU/EEA consumer law on national law invoking the UCT Directive 93/13 and the national implementing contract law and requesting an "advisory opinion" from the EFTA Court, the Supreme Court did not admit those requests.[103] The refusal to refer questions to the EFTA Court has – so far – been based on the argument that clarification is not needed (*acte claire*). The Supreme Court has implied that there was a presumption *de jure* that national legislation is clear and there is no need on external interpretation. The same holds true with regard to cases between financial institutions or legal persons. The highest court has, until now, resolved issues on FX-indexation on the basis of national private law (mainly through contract law, although recent cases show some interaction of consumer law regarding additional guarantees and obligations of information). However, following case 600/2011 and case law on companies, consumers are granted rights to recalculations of illegal FX-indexed loans under general contract law (see below). At the end of 2013, the Supreme Court decided to send a question regarding the compatibility of a CPI-indexed loan with Directive 93/13/EC (case 489/2013, see below) but this case was later withdrawn and resent by the district court. Another judge from the District Court of Reykjavík sent another petition for advisory opinions from the EFTA Court.

b. What were the issues in question? (ie: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)

The most relevant litigation has focused on the illegality of FX-indexed loans under Icelandic law and the necessary recalculation of cars and mortgage loans following partial nullity of contracts. Since the three most important commercial banks of Iceland (Arion/Kaupthing, Glitnir/Íslandsbanki and Landsbanki) and almost all savings banks were put into resolution/liquidation process in 2008/2009 (a process still under way) some issues fall under bankruptcy and/or company law. Complexity from the specific legal framework applicable to the liquidation of financial institutions has, in some instances, deprived consumers from the general protection of contract and consumer law and has led to hundreds of complaints before authorities,[104] see for example cases 226/2012 and 750/2012.

2. Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?

From 1 October 2008 to 20 September 2013 (almost five years) the records on the database of the Supreme Court show 195 cases (some might affect the same parties but deal with separate or interconnected issues). Out of those cases 72 are between individuals and banks, while the others (the majority) are between companies and financial institutions (old or new) or financial institutions between themselves. Out of 72, we selected 36 relevant cases which focused on credit and mortgage loans.

By contrast, if the database is consulted before 1 December 2008 with the same name of the parties, the records show 39 cases, most of them between financial institutions and/or companies, and we found only one case where an individual sued a bank on a problem relating to the release of previous mortgage obligations on the property upon acquisition and payment.[105]

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103 Supreme Court, cases 524/2011 and 576/2011 between two companies and Supreme Court of Iceland, judgment in cases 660/2010, 327/2013 and 328/2013.

104 Ministry of Presidency, Report on the financial position of households, 2013, 32.

105 With regards to litigation before the courts after 2008 on substantial credit and mortgage issues, this data has been obtained by consulting the Supreme Court database www.hæstirettur.is by name of litigants and inserting the names of the four most important commercial banks as well as other financial institutions (the saving banks from Reykjavík (SPRON) and Hafnarförður, financial institutions such as Frjálsi/Drómi, SP-Fjármögnun, Lýsing, BYR and others), while with keywords such as "consumer" "credit" "loans", etc. the research did not deliver complete results due to the lack of uniform terminology and typology of issues discussed.

3. *What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?*

- Litigation on the legality of loans (mostly FX-indexed loans or foreign loans)

We found 20 relevant cases. The Consumer won in four cases (three FX-indexation and one illegal CPI-indexation) and partially won in two cases. Four cases were dismissed for retrial - for inconsistency of legal argumentation (due to the entry into force of Act 151/2010 or because the plaintiff changes legal strategy and does not want to clarify the issue raised). Banks won ten cases (most of them refer to legal foreign loans but last four cases might be testing limits of how far case-law on illegal FX -indexation and legal foreign loans reaches).

- Litigation on additional personal guarantees from third parties (mortgage loans)

Nine relevant cases found. Six cases were won by banks. The consumer won in two cases, in which the expenditure assessment test was wrong- cancellation of guarantee. In one case the consumer won amongst other reasons because assessment was partially inaccurate but not wrong. The Supreme Court does not assess whether the third person providing additional personal guarantee read the underlying document or the outcome of the expenditure capacity assessment or greiðslumat. What seems to matter is whether or not this test provided an accurate picture of the financial capacity of the main debtor to assume future obligations.

- Petitions for a reference from the EFTA Court on the interpretation of national law in the light of European consumer (credit) law

Five relevant cases have been found, three in which the request proposed by the parties is denied (illegal FX-indexed loans) and two recent cases in which the petition from the debtor (consumer or small business) is accepted (concerning CPI-indexed mortgage loan) (EFTA Court cases E-23/13 and E-25/13.

- Other

Three other relevant cases found. Consumers won two cases regarding the main claims related indirectly to mortgage credit but lose additional rights due to interference of procedural law and bank/restructuring process. In one instance the consumer lost a case concerning overdraft credit.

4. *Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?*

Civil procedural law was modified by Act No. 117/2010 to allow some changes regarding *locus standi* of group of individuals defending collective claims (*hópmálsókn*) but imposes responsibility *in solidum* (vs. *pro rata*) in the financial consequences of losing a case: the winner is reimbursed, at least partly, for their legal costs.

For consumer complaints, Act No. 141/2001 on injunction and litigation to protect overall consumer interest (in force since 31 December 2001) allows public interest litigation. This legislation is complemented by the Notification No. 456/2006 and later 1320/2011 on appointed authorities and organisations which are entitled to initiate injunctions for the overall interests of consumers. Now, the Consumers Spokesman (Talsmaður neytenda) and the association of consumers Hagsmunasamtök heimilanna have locus standi to request such an injunction under Act No. 141/2001 as modified by Notification 1320/2011. The same holds true for the Consumer Agency (Neytendastofnun),[106] which has so far not made use of this right.

106 The Consumer Agency is a governmental agency established on 1 July 2005 according to Act No 62/2005. It is responsible for the market surveillance of business operators, the good functioning and transparency of the markets in

a. How are those interests defined?

There is no special definition, it is question left open for the national courts to interpret according to circumstances of the cases on the ground.

b. What are the requirements for such representation?

Requirements are those set by Article 24.1 of Act No. 31/1990 and Act 141/2001(see judgment from Supreme Court of 15 October 2012 in the first case ever tried in Iceland 636/2012 see below next section). The Consumers Spokesman and the Association of Consumers representing consumer interests may ask for an injunction or litigate before the courts even if they have not suffered individual damage or have a direct concern. The Minister of Interior has approved a list of associations with *locus standi* to represent the public interest.

5. In practice, is litigation in "public / diffuse interest" more common than individual litigation?

Individual litigation is the norm since, to date, there has been no case of collective claims brought by consumers before the courts due to the fact that their cases and claims diverge significantly. However possible in theory, in practice litigation in the public interest (i.e. with a prevention-of-damage approach) has proven to be difficult. To the best of our knowledge, "diffuse interest" litigation is not contemplated in Icelandic procedural law.

One case was brought before the Supreme Court by a consumer association (Samtök heimilanna - SH), with the request from the association and the Consumers Spokesman to stop the debt collection of FX-indexed loans for reasons of legal uncertainty concerning their legality and methods of recalculation. In the case 636/2012 the Court ruled that this measure of general interest was not necessary or legally justified under Act No. 141/2001 on interest and indexation since the legal system provides sanctions or compensation for damages to those individuals affected.[107] The Supreme Court nevertheless confirms that this *locus standi* of associations is not restricted to cases with a trans-border or European dimension but can also be used for internal consumer (credit) problems, contrary to the opinion of the district court.

In another case (case 519/2013), the Court decided against the same consumer association SH, which requested a ban on the financial company Lýsing concerning the recalculation and seizure of property on the basis of potentially illegal FX-indexed car loans. The Supreme Court rejected the petition of the association again under Act 141/2001 referring also to Article 24.3.1 of Act No. 31/1990. It concluded that the information provided by the company and the financial reserves set aside by Lýsing to deal with errors of calculation were sufficient for the consumers affected and, as it had previously held, the legal system was regarded as providing sufficient administrative sanctions and/or damages to protect the economic rights of those individuals concerned.

6. Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?

(Contd.)

respect to safety and consumers' legal rights as well as the enforcement of legislation adopted by the Icelandic Parliament for protection of consumer health as well as legal and economic rights. It falls under the responsibility of the Ministry of the Interior. It has the competences to the monitor the application and enforcement of the following legislative acts:

- Act No. 57/2005, on the surveillance of unfair business practices and market transparency
- Act No. 30/2002, on electronic commerce and other electronic services
- Act No. 141/2001 on injunction and litigation to protect overall consumers interest
- Act No. 46/2000, on door-to-door sales and distance contracts
- Act No. 23/1997, on contracts on a timeshare basis
- Act No. 121/1994, on consumer credit
- Act No. 80/1994, on package tours and Regulation 156/1995 on Package Tours

107 "réttarreglur um refsingu eða skaðabætur fyrir röskun hagsmuna gerðarbeiðanda tryggi þá nægilega"

Yes, the national legal framework allows ADR to a certain degree. The Financial Supervisory Authority of Iceland (FME) provides consumers with legal information as well as an option on the enforcement of their rights. It does not have power of arbitration in individual disputes and has no authority to decide on the rights and obligations of parties in this respect or in disputes where the proof of evidence is needed.[108] The Consumer Agency (Neytendastofnun) has more competences than the FME concerning general consumer protection. Individuals can send complaints to this institution. Following the gathering of evidence and due process the Consumer Rights Division issues recommendations or settlements (mediation). Some cases result in formal decisions and bans. The decisions of the Consumer Agency can be appealed to the independent Consumer Appeals Committee.

According to the Consumer Agency, various ADR bodies exist in Iceland.[109] We find five ADR bodies allowed under the legislation on the sale of consumer goods, telecommunications, services of lawyers, rental agreements, apartment buildings and six ADR bodies that are optional for economic operators (insurance, banks, travel, craftsmen, dry-clean services, and dental services). There are two independent committees, which were created by collaboration between consumer associations and the business industry which fit into this category of ADR: the Insurance Complaints Committee and the Complaints Committee on Transactions with Financial Firms,[110] which has operated since 2000. They operate under the supervision of the Financial Supervisory Authority (FME) and constitute a voluntary arbitration scheme open for both individuals and business which does not substitute itself to the courts.[111]

7. Do consumers make use of out-of-court settlement procedures?

Yes. In fact, the numbers of cases resolved through out-of-court settlement procedures has increased since the financial crisis.[112] The number of cases was steady in between 2001 and 2008; 21 cases per year on average. In 2009 the cases increased to 66 but fell again to 44 in 2010. In 2011, it increased significantly to 115 and to between 178 and 201 in 2012 (data still not definitive). This increase probably goes hand in hand with an increase in litigation in general.

If yes:

a. Which ones?

Apart from the possibility of bringing a complain to the Administration (FME and Consumer Agency) consumers may use the ADR independent committee (arbitration scheme) set up by the industry in collaboration with consumer association, namely the Insurance Complaints Committee and the Complaints Committee on Transactions with Financial Firms.[113]

b. What is their success rate?

The success rate for individuals (both consumers and businessmen against financial institution) was around 55.5% in 2012.[114] In general the legal framework on access to justice for consumers concerning economic rights and disputes with financial institutions needs to be ameliorated as it is not functioning as effectively as in other Nordic countries. The ad hoc Committee nominated to evaluate consumer protection in financial markets concluded in April 2013 with the following recommendation on this point: there is a need to reinforce the competences of the FME concerning disputes between

108 Ministry of Presidency, Consumer protection in financial markets, 2013, 78.

109 Neytendastofa ("Consumer office") website, 2008.

110 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 89.

111 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 95.

112 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 90.

113 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 90.

114 Ministry of Presidency, Report on consumer protection in financial markets, 2013.

individuals and financial institutions, a new Ombudsman for consumers should be created and an improvement of the legal framework for public interest litigation should also be sought. For the time being consumer protection in Iceland has gravitated towards the notion of information given to parties rather than regulation and control of abusive practices.[115]

c. What are the issues?

Some cases exist where consumers have used the out-of-court schemes to solve their disputes with the financial institutions (car loans and car leasing contracts). According to the Administration[116] we find a total of sixteen decisions from the Consumers Agency since 2008 related to the protection of consumers in the financial markets (five of them concerning FX-indexation of car loans or car leasing contracts). Other four cases relate to the commercialization of voluntary additional private pension schemes. It is unclear whether any of this decision was adopted following the public initiative of the Administration or whether they derived from claims started by private parties. 50% of claims dealt by the Administration do not concern claims from consumers but claims between commercial companies for issues of advertising or competition.[117] This confirms one of the main conclusions of the Administration: a lack of effective administrative institutional framework for the protection of consumers against abusive clauses.

8. Are there special bankruptcy courts? What is their role?

There are no special bankruptcy courts, ordinary courts oversee bankruptcy of both individuals and companies.

XIV. Impact of the crisis on litigation

1. Has there been an increase in litigation since the financial crisis? And how many mortgage agreements were challenged in out-of-court or judicial proceedings before and after the crisis?

Yes, since October 2008 there has been a significant increase in litigation concerning consumer credit, car and mortgage loans and, more recently, student loans. Litigation has also taken place on issues of company law, law of contracts and obligations between companies, companies and financial institutions. Financial institutions have also solved some difficult issues linked to the resolution and winding-up of failed banks before the courts. Our data refers to the end of October 2013.

a. How many mortgage agreements were challenged in out-of-court or judicial proceedings before and after the crisis?

Fifteen mortgage agreements were challenged after the crisis (number of cases litigated is larger) in cases litigated between banks and consumers. Nine cases in which additional guarantees given by third parties on mortgage agreements were challenged after the crisis. Before the crisis, litigation in this field was marginal.

b. What are the issues challenged? In which legal field?

See answer to XIV.1.c.

c. What were the predominant issues (before and after 2008)

The main issues in consumer or mortgage loan agreements are the legality and legal effects of possible illegality of FX-indexed loans and CPI-indexed loans. Litigation has also been important with regards to the validity and execution of additional guarantees given by the third parties on mortgage loans.

115 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 75.

116 Ministry of Presidency, Consumer protection in financial markets, 2013, 76-77.

117 Ministry of Presidency, Consumer protection in financial markets, 2013, 76-77.

- Illegality of FX-indexed loans / legality of foreign loans

According to the Act on Interest and Price Indexation No 38/2001, it is permissible to grant loans in foreign currency but not to link obligations denominated in Icelandic krónur (ISK) to foreign currency exchange rates. On 16 June 2010, the Supreme Court of Iceland handed down two judgments that declared that two car lease agreements between financial institutions and private individuals were actually loan agreements containing illegal exchange rate linkage clauses.[118] While these judgments set a clear judicial precedent for a number of exchange rate-linked loans, its effects were uncertain for many other different loans (i.e. house loans). It has been especially difficult to clarify the consequences of the partial nullity with regard to the recalculation of the outstanding due balance and underlying interest rates. Initially, the interests agreed by the private parties (i.e. Libor) were modified on the basis that a "foreign" interest (such as LIBOR) cannot survive the declaration of illegality of FX-indexation and that the Central Bank interests should be applied instead. The Supreme Court has, however, changed its case law and has moved away from the *ex tunc* effects (see below).

Following a letter of formal notice from the EFTA Surveillance Authority to Iceland on 19 April 2012, the Supreme Court made a further distinction between legal loans in foreign currencies and illegal FX-indexed loans in local currency (ISK). In June 2012 the Supreme Court ruled that foreign-denominated loans of Islandsbanki (previously Glitnir) were legal.[119] It argued that there was a formal difference between loans where the amount is stated in foreign currency and FX-indexed loans where the amount of credit is stated in local currency (ISK) but indexed to a foreign currency. For the Supreme Court it did not matter that the real payments were done in local currency as it looked at the formal denomination of the amount of credit in the contract.[120]

The Central Bank of Iceland and the Financial Services Authority have issued guidelines for financial undertakings on the treatment of loans linked to currency exchange rates, influencing the following case-law on both car and house loans.

- Recalculation of illegal FX-indexed loans: Central Bank interest rates vs contractually agreed rates

On 16 September 2010, the Supreme Court clarified the question of the interest applicable following the partial nullity of FX-indexed car loans. It stated that the interest rates specified in the FX-indexed contract agreements concerned should be set aside in favour of the interest rates of the Central Bank for ISK-denominated bank loans at any given time (non-indexed loans). These interest rates are regularly published by the Central Bank of Iceland.

At the end of December 2010, the Icelandic Parliament adopted Act no. 151/2010 on the illegal FX-indexed loans stipulating how individuals' FX-linked mortgages and motor vehicle loans should be recalculated. The declared aim was to ensure non-discrimination among individuals, irrespective of whether a contract had been deemed illegal or not. In the following months, financial institutions converted FX- indexed motor vehicle loans in accordance with the interest rates published by the Central Bank of Iceland, as well as giving households with residential mortgages the option of converting loans into legal CPI-indexed or non-indexed loans (new choice). The argument was that the effects of the Supreme Court case law for FX- indexed loans were to be ex tunc in all instances with

118 Cases no. 92/2010 and 153/2010.

119 Case no. 524/2011.

120 This stance has been confirmed in subsequent cases 3/2013, 332/2013, 499/2013 even though consumer associations have argued that the method of payment (in ISK) should be also relevant to determine illegality as well as all documents from the banks regarding supply of credit and potential manipulation of the markets (an argument rejected implicitly by the Supreme Court in case 699/2010 where access to documents from the bank is denied and individuals condemned to pay for cost of litigation of the bank).

no derogation possible (that is to say recalculation of the loans with the interest of the Central Bank of Iceland from the contractual date).[121]

Following re-calculation, thousands of consumers protested against Act no. 151/2010 and the ex-tunc effects of recalculation. They argued that the imposition of Central Bank interest rates expropriated their economic rights regarding the past payments made in good faith (as interest rates had risen up to 21% at a certain point). On 15 February 2012, the Supreme Court declared the partial unconstitutionality of Act 151/2010 concerning the retroactive recalculation of interest detrimental to individuals on the basis of the protection of private property against expropriation without due guarantees. The case no. 600/2011 concerned the validity of so-called full-payment receipts and the rights of the financial institutions to claim unpaid interest on the basis of the retroactive effect of Act 151/2010. The Court concluded that an illegal FX-indexed loan could not lead to additional payments or penalties for previously (un)paid interest rate, if a receipt for full payment of the loan -as it stood at that time- had been duly accepted by the financial institution at the due dates. Thus, the consequences of the illegality and recalculation of the loans concerning due Central Bank interest are *ex nunc* but not *ex tunc*.[122]

On 18 October 2012, the Supreme Court of Iceland confirmed its position on the retroactive recalculation of interest for illegal FX-indexed loans in case *Borgarbyggd*.[123] The judgment relates to a dispute on the interest rate used in the recalculation of an FX- indexed loan agreement concluded between the municipality of Borgarbyggd and the Arion Bank (former Kaupthing). The judgment follows the precedent in case No. 600/2011 regarding the value of final receipts of payment. It casts light on how illegal FX-indexed loans should be calculated in the future. Both cases involve long term loans with illegal FX- indexation that have been duly paid for a long period of time in accordance with the payment bills sent to the borrowers. In both cases the Court concluded that particular requirements allowed departure from the main principle of the law of obligations that the creditor may demand additional payments retroactively from the debtor in relation to unpaid contractual interest.

On 30 May 2013, the Supreme Court of Iceland handed down a new ruling in the case Plastiðjan[124] concerning the bases and results of recalculation. It concerns a motor vehicle loan agreement with illegal exchange rate indexation concluded in 2007 between a company and the bank Landsbanki. The loan was recalculated in 2011 with the interest rates determined by the Central Bank of Iceland (according then to Act nr. 151/2010). The Supreme Court found that following recalculation the bank was not authorised to require payments in addition to instalments made during the period when the loan was being paid off in a timely manner, since all conditions the Court had set in order to benefit from previous case-law had been fulfilled.

Litigation is still ongoing on some difficult cases concerning FX-indexed loans.[125] Consumer associations and the Debtor's Ombudsman consider that most difficult issues on recalculation of illegal FX- indexed loans have now been resolved. In contrast, financial institutions claim a lack of

121 On 9 June 2011, the Supreme Court took a similar approach in the so-called Motormax case 46 (Case no. 155/2011). In that decision, an FX loan agreement between a legal entity and a financial institution was declared illegal for the first time, extending the scope of the doctrine on partial illegality of car loans to loans falling under company law.

122 Despite the importance of this case for the re-structuring of household debt, a number of questions remained unanswered, for example the legality of different contract forms used by the financial institutions, the effect of debt relief measures (both publicly adopted and privately agreed), the validity of some payment receipts, and the methodology to be used for difficult cases where recalculation was not simple. Therefore, after the Supreme Court judgment in case no. 600/2011 concerning the effects ex nunc of the recalculation of due interest for illegal FX-loans, eleven cases were selected by the three major banks with the collaboration of the Ombudsman for Debtors to clarify further issues. It was agreed that the cost of this litigation would fall on the banks and not on the individuals affected. Some of these cases have been already adjudicated for the benefit of due recalculation of credit towards both consumers and companies. Others are still pending.

123 Case no. 464/2012.

124 Case no. 50/2013.

125 IMF, IMF Country Report 13/256, 2013, 15.

legal certainty for loans that do not fit the precedents (i.e. where the debtor defaulted or benefitted from debt-mitigation measures such as freezing of payment of principal or payment of ISK 5,000 ISK per million which was offered during some years where legal uncertainty existed).

- CPI-loans

An important case of 24 April 2013 declared the nullity of a CPI-indexation clause in a car loan (case 672/2012). It was the first time that the Supreme Court applied consumer credit law (Act no 21/1994) and dealt with the consequences of lack of transparency and clarity of obligations in a consumer contract. Neither the contract nor the payment plan contemplated indexation of the car loan nominated in ISK and the variable interest rates applicable. In these circumstances, the Court found that the creditor cannot claim respective payment afterwards. Lýsing had argued that the debtor - by not protesting at the beginning- accepted the methodology of calculation. Lýsing lost the case and had to refund what the individual had paid in excess.

Some new cases are being dealt by district courts on the potential illegality of some CPI-indexed loans (*verðtryggt*) on the basis of arguments of consumer and contract law (ie. lack of due disclosure of financial obligations under Act no. 121/1994 on consumer loans incorporating European law).

Three cases concerning indexation of mortgage loans are still open. First, the Consumer Association *Samtök heimilana* brought a case against the House Financing Fund (*Íbúðalánasjóður*) before the District Court of Reykjavík on the 18 October 2012. The judge's decision of 2 May 2013 to dismiss the action on formal grounds has been appealed to the Supreme Court.[126] The arguments of the association are built on Act No. 121/1994 on consumer loans and EEA consumer law (Directive 93/13/EC unfair terms in consumer contracts and requirements of transparency and disclosure of financial obligations). A similar case is being tried by private parties supported by the trade-union of Akranes against the bank Landsbankinn where other issues are also being tested in the light of the MiFID.[127] A petition to send the case to the EFTA Court was put forward by the parties in May 2013 and was finally accepted at the end of October 2013. The Supreme Court sent a reference to the EFTA Court for an opinion on the legality of a CPI-indexed mortgage (see above, case 489/2013) but withdrew the petition afterwards. Two cases are pending before the EFTA Court (E-25/13 sent initially by the Supreme Court and then re-sent by the District Court of Reykjavík and E-27/13 also sent by the District Court of Reykjavik)

- Additional guarantees by third parties on mortgage contracts

There have been other cases where the litigation revolved around the additional guarantees given by third parties to secure a mortgage loan in connection with consumer law. In cases 4/2013 and 127/2013 the Supreme Court decided to declare null and void the guarantee given by a third party on a loan taking into account defects in the contracting stage (lack of information and due consent of the individual providing guarantee).[128] This was decided under Art. 36 of Act No. 7/1936 of contract law. In other relevant cases 213/2012 and 343/2013 the Supreme Court decided, nevertheless, that the breach of information duties did not comply with all requirements set by national legislation and did not cancel the guarantee given.[129]

2. Did the Aziz ruling have an impact on national legislation / legal framework?

126 Ministry of Presidency, Report of consumer protection in financial markets, 2013, 61.

127 Ministry of Presidency, Report of consumer protection in financial markets, 2013, 61.

128 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 54.

129 Ministry of Presidency, Report on consumer protection in financial markets, April 2013, 59.

This judgment has not had a direct impact yet on national legislation or on the execution of distressed sales (not mentioned in the Report on consumer protection in financial markets, 2013). No case has been adjudicated so far in the light of Article 36 of contract law (letters a-d) and the UCT 93/13/EC.[130]

a. Are there cases before national courts dealing with issues that also arose in the Aziz case?

A similar case can be referred to (693/2011) where the company Drómi took sued a consumer who had given a guarantee as a third party in a mortgage contract. The company (whose goal it is to maximise the assets of the failed saving bank SPRON and the financial institution Frjálsi) won the case. The Supreme Court ruled that it could initiate procedure for seizure of property asking for the bankruptcy of the guarantor even if the debtor was supposedly under protection of governmental policy and Act 101/2010 (Debtors Ombudsman). The file is still to be closed by the Administration. The private party does not invoke the application of *Aziz*.

A case in which the *Aziz* ruling does play a role could be case Z-6/2013 of the South District Court. The Home Owner's Association is currently preparing an opinion that analyses the legal framework, including the UCT 93/13 and the *Aziz* case. Preliminary results - disclosed to us in an interview - show that the conditions in the *Aziz* case are at least similar to the ones in Iceland. The first possibility to have potentially unfair terms reviewed is through an annulment case after the enforcement procedures. This case is expected to land before the Supreme Court.

b. What was / is considered an unfair contract term in the national court rulings before and after Aziz?

So far the Icelandic courts have not engaged in an analysis of unfairness of contract terms under the influence of Directive 93/13/EC (Art. 36 a-d of Act 7/1936 on contract law). This refers to both consumer credit and mortgage. Resolution of the cases E-23/13 and E-25/2013 is pending.

c. Did Aziz have any other impact on national legislation / legal framework (ie. in the field of procedural law)? What are those impacts?

No. In fact, there seems to be a practice of Icelandic authorities and judges to not examine ex officio potentially abusive clauses, with a presumption de iure that the creditor is complying with the legal framework. For example, in case 620/2013, in which the consumer had not paid the last instalments of the mortgage and could not pay outstanding debt, the Supreme Court decided that the potential illegality of a recalculation of an illegal FX-indexed loan would not postpone the starting of the bankruptcy procedure. It remains open whether potential abuse will be claimed later. In another case referring to car loans/leasing, the consumer association *Samtök heimilana* tried -through the petition of an injunction- to ban the enforcement of the of (illegal FX-indexed) loans from the company Lysing on the basis that there was a legal uncertainty on their calculation method and that consumers should not lose their economic rights as the company might face financial difficulties reimbursing them in the future for miscalculation of claims and overdue interest payments. The Supreme Court rejected the petition (see case commented above) on the basis that the Icelandic legal system provides a set of remedies ex-post to satisfy damage for individuals affected in these circumstances.

130 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 69-70. Consumer associations have, unsuccessfully, invoked the importance of this case in order to pressure financial institutions to comply with European consumer credit law when enforcing defaulted loans on properties (following re-calculation of illegal FX-indexed loans and more recently CPI-indexed loans). This has been a deemed a surprising lack of effectiveness of the Icelandic legal system as applied and interpreted by national courts (even when the private parties invoke their rights as consumers under national and EEA law), taking into account the financial collapse of the banks in 2008 (Ministry of Presidency, Report on consumer protection in financial markets, 2013, 94). However, neither the legislator nor the judiciary are not directly bound by the case-law of the CJEU on the basis of the EEA Agreement (Mendez Pinedo and Hannesson, The authority of European law: Exploring primacy of EU law and the effect of EEA law from European and Icelandic perspectives, Lagastofnun, 2012).

3. Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework? Elaborate.

The legal opinion requested from the EFTA Court in case E-25/13 (HR. case 489/2013) concerning the question whether Íslandsbanki broke the law when it sold a CPI-indexed (inflation-linked) mortgage to his client might change the practice of not taking into account European cases. The different questions asked of the EFTA Court initially by the Supreme Court[131] and by the District Court of Reykjavík[132] refer to the compatibility of the domestic legislation with EEA law[133]. The first question referred initially mentions in general "provisions stating that the instalment repayments are to be linked to a pre-determined index", expression which is unclear as it leads to confusion[134]. In this sense, the first and seconds question referred by the District Court in case E-27/13 are better formulated.[135] These are all novel questions for the EFTA Court. The last question in both cases refer to the mandatory nature of the sanction prescribed by Directive 93/13 for unfair terms) (non-binding), a question already dealt with by the CJEU[136].

Interestingly, the first case does not refer directly about the obligation of previous disclosure of the total cost of credit with the European standard formula under Directive 2008/48 (applicable to mortgage credit in Iceland). This is done in the following case E-27/13 sent by the District Court of Reykjavík where the judge specifically asks whether it is compatible with EEA consumer law to have inflation calculated as 0% in total amount of credit given, total cost of credit and plan of payments according to the European rules set by Directive 87/102 and 48/2008 on consumer credit[137].

The most important arguments that need to be examined by the courts on consumer and mortgage credit in Iceland in the light of European law are the following:

131 EFTA Court, case E-23/13 *Gunnar V. Engilbertsson v Íslandsbanki hf.* pending, later re-filed as case E-25/13.

132 EFTA Court, case E-27/13 *Sœvar Jón Gunnarsson v Landsbankinn hf*. pending.

133 See on the nature of EEA law and enforcement of EEA law by Icelandic domestic courts Hannesson, O.I. (2013). Giving Effect to EEA Law - Examining and Rethinking the Role and Relationship between the EFTA Court and the Icelandic National Courts in the EEA Legal Order. Fiesole: European University Institute. Doctoral thesis.

134 Question 1 in case E-23/13. Is it compatible with the provisions of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts if the legislation in a State which is a party to the EEA Agreement permits contracts between consumers and suppliers for loans to finance real estate purchases to contain provisions stating that the instalment repayments are to be linked to a pre-determined index?

135 Question 1 in case E-27/13. Is it compatible with the provisions of Council Directive 87/102/EEC on consumer credit, as amended by Directive 90/88/EEC and Directive 98/7/EC, that when a credit agreement is made, which is linked to the consumer price index in accordance with an authorisation in enacted legislation, and the sum loaned therefore changes in accordance with inflation, the calculation of the total cost of the credit, and of the annual percentage rate of charge, which is shown to the consumer when the agreement is made, is based on 0% inflation, and not on the known rate of inflation on the date when the loan is taken?

Question 2 in case E-27/13. Is it compatible with the provisions of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts if the legislation in an EEA State permits the inclusion of provisions in a consumer contract, stating that repayments of the loan are to be linked to a predetermined index?

136 Question 6 in case E-23/13. Does a State that is party to the EEA Agreement have the option, when adopting Article 6(1) of Directive 93/13/EEC, of either prescribing in domestic legislation that unfair contract terms within the meaning of Article 6(1) of the Directive may be declared non-binding on the consumer or prescribing in domestic legislation that such terms shall at be non- binding on the consumer at any time?

Question 6 in case E-27/13 is identical to question 6 in case E-23/13.

137 The Agency for consumer protecion in Iceland (*Neytendastofa*) has recently adopted a decicion in which it declares that the bank Islandsbanki violated European/national consumer law provisions when it calculated the cost of credit of a mortgage loan taking into account 0% inflation - Neytendastofa. Decision nr. 8/2014 of 27.2.2014. The agency declares the implementation of the indexation in practice a violation of Act nr. 121/94 on consumer credit applicable to mortgage credit since 2001 and Act nr. 57/2005 on unfair commercial practices with no-binding legal effects towards the consumer. The decision is available in Icelandic at: http://www.neytendastofa.is/library/Files/Kaerunefnd-lausafjar--og-thjonustu/%C3%81kv%202014_8.pdf

- the need to inform the consumer of the total cost of credit through the APCR formula of Directives 87/102 and 48/2008
- the question of whether indexation regulated by law constitute or not abusive clause in light of Directive 93/13,
- the necessary proactive role of the national judges in the assessment of abusive clauses even though the private parties have not raised the argument,
- the consequences of potential illegality of indexation clauses when European requirements are not respected in the contract (after entry into force of new Act 33/2013),
- the interpretation of national credit law under European consumer law when the legislator has extended the scope of Directives on consumer credit to mortgage loans.
- the mandatory nature of the declaration of nullity of abusive clauses in European law and the lack of powers of the national judges to amend the contracts
- the potential application of the case-law of the CJEU to the Icelandic legal order via the EEA Agreement (i.e. Influence of case RWE as a precedent to determine the legality and limits of the CPI- indexation practice).
- the lack of effective administrative supervision in Iceland on Directive 93/13 (Article 7)

It is possible that the EFTA decides to reply to as many issues as possible, regardless of the formulation of the questions done by the Icelandic national judges. In this sense, there might be a potential indirect effect of the EU case law and jurisprudence through the EFTA Court through the EEA Agreement and/or through informal channels of judicial research and dialogue.

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

The Icelandic state has taken various debt-restructuring measures and attempted to simplify bankruptcy procedures for consumers (see above). Together with the re-calculation of illegal FX-indexed loans (a court-led development), those debt-restructuring measures have had an impact on the levels of indebtedness of Icelandic consumers. Those measures are:[138]

October 2008

- Moratorium on foreclosures
- Temporary payment freezing of foreign-denominated loans

November 2008

- Payment smoothing of ISK mortgages introduced by law
- Third-pillar pension pay-outs, later expanded
- Increases in mortgage interest subsidies

March 2009

- Payment smoothing of foreign-denominated mortgages introduced by law

May 2009

138 Main policy and legal interventions in Iceland since 2008 – source Central Bank Report WP 59.

- Act on Temporary Mitigation of Residential Mortgage Payments

October 2009

- Law on measures for individuals, households, and corporations due to the banking and currency collapse providing a framework for decentralised debt restructuring
- Agreement on offering payment smoothing for foreign-denominated motor vehicle loans

November 2009

- Payment smoothing applied to all indexed ISK mortgages unless households opt out

June 2010

- The Supreme Court rules that indexation of motor vehicle payments in ISK to changes in currency exchange rates is illegal

August 2010

- Office of the Debtor's Ombudsman created to oversee and provide advisory and mediation services related to debt mitigation procedures
- Measures introduced for households with two properties for personal use

September 2010

- Supreme Court rules that interest should be calculated on illegal foreign-denominated motor vehicle loans in accordance with general interest rates on ISK bank loans, published on the Central Bank of Iceland website

December 2010

- Law on recalculation of illegal foreign-denominated loans to Icelandic households
- Adjustments of mortgage debt to 110% of the underlying collateral value
- Expansion of the voluntary debt mitigation framework
- Enhanced and more progressive tax rebate on interest
- Special interest rebates for the years 2011 and 2012

In mid-May 2014, a new governmental plan was adopted for debt relief by the Parliament. It applies only to inflation-indexed loans and amounts to a total of ISK 150 billion (around 8% of estimated Icelandic GDP in 2014) and covers a timeframe from mid-2014 for up to four years. It will be funded by an increase in the levy on financial institutions.[139] The government's plan consists of two parts: (1) a direct write-down of inflation-indexed mortgage principal of up to 13%, amounting to a total of ISK 80 billion over a four-year period; and (2) a 6% tax exemption that can be used to pay down mortgage debt of ISK 70 billion over a three-year period. The tax exemption relates to payments that households (and their employers) would otherwise have been able to make towards their private pension funds. According to the government, the plan will lower the outstanding mortgage principal by up to 20% by 2017 and will be available for 80% of Icelandic households. Earlier mortgage relief transactions will be taken into account as the maximum debt relief under (1) is ISK 4million per household (around 20K GBP), while option (2) is limited to a total of ISK 1.5 million (around 8,000 GBP) over the three-year period.

139 This plan has been subject to criticism. The IMF did not encourage such a policy due to the cost of those general measures and the lack of effectiveness to help those most in need on its Report on Iceland July 2013. The OCDE told Iceland to target its mortgage relief efforts at low-income households, fearing broad tax cuts could undermine public finances on its latest country report (Iceland) of 2013. The Central Bank of Iceland in 2012 also advised strongly against general debt relief (which they call across-the-board write-offs) which would not target those in distress, could be costly, ineffective, jeopardize financial stability and push up inflation.

The government is also working in the abolition of the indexation of credit for new loans although the Committee designated ad hoc for this task declared in January 2014 that this goal was unattainable in the short term due to the consequences on the financial and private pension systems.

2. *Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?*

The fields of law are: consumer credit, bankruptcy law, and general contract law that are affected by debt mitigation and re-structuring measures implemented after the financial crisis in order to alleviate the debt burden.

3. *What are the changes in particular? Focus on consumer credit and mortgage law.*

The overwhelming majority of changes in legislative and policy framework concerned the re-structuring of loans and debt mitigation (see answer to VI.1). Implementing the CCD 2008/48 the new Act on consumer loans no. 33/2013 contains several changes to the previous law, i.e.:

- The Act now includes "small loans".
- The Act includes interest rate restrictions which means for example that nominal interest on small loans are reduced from 468% down to 44.5% on a two week loan of ISK 60.000.
- Creditor information requirements are elaborated and much more detailed.
- Loan broker obligations and information requirements are stipulated.
- Loan worthiness and credit worthiness assessments are required.
- The borrower will now have a right of withdrawal.
- A special calculation rule when loan is paid up before payment day and the fee the creditor can claim.
- Clearer provisions on overdraft as well as clear provisions on the consumer´s right when a seller provides a loan.

Bankruptcy law was also changed, with a view to facilitating bankruptcy for individuals. With Act No. 23/2009 the Act on Bankruptcy was changed, for example, so that that claims asserted in the bankruptcy proceedings are prescribed (German: *Verjährung*) two years after the termination of the bankruptcy proceedings, instead of the previous four years. With regard to *locus standi* of consumer associations, Notification 1320/2011 on appointed authorities and organizations who are entitled to initiate injunctions for the overall interests of consumers allows the Consumer Agency (*Neytendastofnun),* the Consumers' Spokesman (Talsmaður neytenda) and the association of consumers *Hagsmunasamtök heimilanna* to seek an injunction in consumer interest.

4. *When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

The changes elaborated upon in this study were mainly the result of policy initiatives in Iceland after the financial and economic crisis (see Table 33). As stated in the section entitled "litigation", both EU legislation and case law of the CJEU have had surprisingly little impact on Icelandic legislation and jurisprudence. Changes in consumer law were made in compliance with the CCD 2008/48.

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, ie with regard to savings?)*

Apart from the following first three reasons that are mentioned in the reports of Central Bank and ministries, there are other, country-specific phenomena (last three), which are not always properly analysed and assessed:

- the lack of firm regulatory control on financial practices carried by the banks before the crisis (i.e. illegal FX-indexation of car and house loans).[140]
- collapse and necessary re-construction of the domestic financial sector.
- cost and volatility of a micro-currency[141]
- the structure of the most usual loans (CPI- indexation) which reflects unpredictable cost of credit leading to over-indebtedness.[142]
- General use of student credit loans to finance graduate and post-graduate education through the State funded mechanism LIN (student grants indexed to CPI) which add to the burden of households.
- the historically high cost of credit[143] reflecting the size of the market and high inflation.

It is evident that the difficulties in resolving problems over-indebtedness derive from the interconnectivity of consumer credit and mortgage agreements with economic, financial, and monetary policy. Price-indexation (both FX- and CPI) of loans, reflecting the problems of the authorities in their 30-year fight against inflation and the constraints of a micro-currency, seems highly problematic not only in the light of European law but also with regard to its economic rationale. Recent research has shown that CPI-indexation do not reduce or stop inflation, but – on the contrary – directly contributes to the banking system's monetary expansion rate and thus increase the inflation rate to which they are linked.[144]

Together with the revision of the financial framework under way, there should be a policy promoting private saving rather than expenditure. The authorities need to reconsider the role of the House Financing Fund, the Student Loans Scheme and the assets and investments of private pension funds in terms of sustainability and generational justice.

Private individuals and consumer organizations have complained to the European Commission, the European Parliament, and the ESA on the deficit of consumer credit/mortgage protection in Iceland under the EEA legal order. Their claims concern the lack of enforcement powers of the Consumer Agency and the Financial Supervision Authority as well as the practice of national courts (especially the Supreme Court with only one exception to this general rule) to by-pass specific legislation in favour of general contract law (which produces effects both for private individuals and companies). Individual attempts to send legal questions to the EFTA Court have often been denied. Moreover, the

140 Ministry of Presidency, Report on consumer protection in financial markets, 2013, p7.

141 Central Bank of Iceland, Report on the monetary policy choices for Iceland ("Valkostir Íslands í gjaldmiðils- og gengismálum").

142 Association of financial institutions (SFF), Necessity or choice? Indexation, interest and inflation, 2012.

143 Ministry of Presidency, Report on consumer protection in financial markets, 2013, 29.

144 Research done by Jack Mallet "An examination of the effect on the Icelandic Banking System of Verðtryggð Lán (Indexed-Linked Loans)" available at: http://arxiv.org/abs/1302.4112.

implementation of consumer protection directives has been delayed. For example, Iceland has been condemned by the EFTA Court on 6 December 2013 (case E-12/13) for not implementing in due time Directive 2009/22/EC of the European Parliament and of the Council of 23 April 2009 on injunctions for the protection of consumers' interests.

In conclusion it can be said that on the one hand, it is true that Iceland is a leader in Europe in providing temporary debt-relief and debt-discharge to over-indebted households. On the other hand, this is necessary given the extent of indebtedness and over-indebtedness as well as FX-and CPI indexation of consumer loans. Further research is needed on the topic to clarify the interaction between the Icelandic consumer credit and mortage law and the EU/EEA European framework taking due consideration of the most recent case-law of the ECJ (i.e. *Aziz*, *RWE*). The recent petitions to the EFTA Court from the Supreme Court and the district court of Reykjavík to interpret and clarify important issues on CPI-indexation of loans are an important step in this direction.

ROMANIA

Madalina Moraru[1] and Beatrice Andresan-Grigoriu[2]

Preliminary Information

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

The concepts are not defined by legal instruments, soft law or national jurisprudence. However the word "indebtedness" is used by the National Bank of Romania (NBR) in policy papers and surveys (e.g. Annual Reports, and Financial Stability Reports). The term "indebtedness" is used to refer to any situation arising from contractual loan obligations, regardless of the type of credit agreement.[3] Article 13 of Regulation no. 17/2012 of the NBR concerning conditions of indebtedness defines the "degree of indebtedness" as the ratio between the total value of obligations arising from loans and other financing agreements and the value of eligible income (that is the income left after deducting subsistence expenses from the total value of the income). The common terms used by the NBR's publications with a similar connotation to "over-indebtedness" are "overdue loans'', "overdue payments ratio'', "non-performing credit'', "defaulter'' (the latter is usually used in the Monthly Bulletins of the NBR). In addition, the NBR Financial Stability Report also uses the term "arrears" which is defined as payments overdue for more than 90 days.[4]

2. *Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?*

The term "consumer vulnerability" has not received a definition specific to the financial sector. Article 4(2) of Law 363/2007[5] entitled *Unfair Commercial Practices* includes a reference to "vulnerable groups of consumers" as potential addressees of commercial practices in general, and part of the definition of "unfair commercial practices". This provision mirrors the content of Article 5(3) of Directive 2005/29 concerning unfair business-to-consumer commercial practices and stipulates that a clearly identifiable group of consumers who are particularly vulnerable to the practice or the underlying product because of their mental or physical infirmity, age or credulity in a way which the trader could reasonably be expected to foresee, shall be assessed from the perspective of the average member of that group.

The NBR Reports on Financial Stability refer to "indebtedness", and especially in foreign currency, as a vulnerability of the household sector.[6]

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3 Official Journal of Romania Part I, 855, 18.12.2012.

4 See Financial Stability Report 2011, p.100.

5 Law no. 363/2007 on combating unfair trade practices in relation to consumers and harmonization of regulations with EU legislation on consumer protection published in the Official Journal of Romania, Part I, 899, 28.12.2007.

6 See NBR Financial Stability Report, section 5.2.1, p.102; NBR Financial Stability Report of 2013, section 5.2.1.

3. Is the term "poverty" or "low-income consumer" defined in the national legal order?

No.

II. Numbers on over-indebtedness

1. How many consumers are considered "indebted" in the country? (since 2000)[7]

Table no.1

Year	Number of ''indebted'' consumers
Dec 2008	4,139,250
Dec 2009	4,070,031
Dec 2010	3,929,726
Dec 2011	3,791,204
Dec 2012	3,809,976
Sep 2013	3,662,835

Source: NBR (reply to questionnaire 14.11.2013)

Total credit to households per capita (in thousands of EUR): 1996 – 0.065; 1997- 0.008; 1998 - 0.010; 1999 - 0.006; 2000-0.007; 2001 - 0.013; 2002 - 0.027; 2003- 0.084; 2004- 0.139; 2005 - 0.269; 2006- 0.538; 2007- 0.920; 2008- 1.146; 2009 - 1.101; 2010 - 1.117; 2011 - 1.126.

Total credit to households per capita (in thousands of national currency): 1996 – 0.034; 1997- 0.007; 1998 - 0.013; 1999 - 0.012; 2000- 0.016; 2001 - 0.036; 2002 - 0.094; 2003- 0.346; 2004- 0.549; 2005 - 0.989; 2006- 1.820; 2007- 3.318; 2008-4.611; 2009 -4.665; 2010 - 4.761; 2011 - 4.869.[8]

Between 2003 and 2006, household debt to financial assets doubled. Household bank loans to GDP tripled over the same three year period and increased eight-fold between 2002 and 2006. Household credits from the banking sector have grown approximately 80% per year between 2004 and 2007. The expectations of growth of income, the prospect of EU accession, and actual increase of incomes contributed to this increase.[9] Furthermore, in 2005 the NBR anticipated the problem of over-indebtedness that consumers who contracted credits in this period would experience after the financial boom.

In 2006, "household loans grew at a pace faster than that recorded in December 2005 (175% in real terms). Among the factors that accounted for this development were: (i) strong demand; (ii) increase in household income; (iii) favourable macroeconomic developments in recent years (economic growth, lower inflation, domestic currency appreciation); and (iv) increased competition in the banking sector, which affected the interest rates on foreign currency-denominated loans and, in particular, on loans in domestic currency. Non-bank financial institutions made a substantial contribution to the increase of competition on the credit market."[10]

By the end of 2008, household debt represented approximately 20% of GDP.[11] Furthermore, according to the NBR Report on Financial Stability, the weight of household loans in total private loans reached a historical peak of 42.1% in 2008. The determinants were the same income dynamics and optimistic

7 For more details see Chart 10.5.1 of the National Bank of Romania Monthly Bulletin no. 12/2013.

8 Based on the ECRI Report on Lending to Households data (1995 – 2011).

9 NBR Financial Stability Report of 2006, p. 12.

10 NBR Financial Stability Report of 2007, p. 19.

11 World Bank Diagnostic Review of Consumer Protection and Financial Literacy in Romania, July 2009, pp.1 and 11.

expectations of future income, the need of endowment with durables and the household-oriented policies of the banks.[12]

The total level of debt in December 2008 was five times higher than in December 2004.[13]

In 2009 the number of consumer credits dropped due to low GDP and a high unemployment rate limiting access to credits to 11.8%.

In 2011, according to the NBR Financial Instability Report, a large number of individuals (about 0.45 million) borrowed from both banks and non-banking financial institutions (NBFI). Such individuals hold, on average, three loans (two with banks and one with NBFIs) and are the riskiest category of debtors.[14]

In June 2011, approximately 4.2 million individuals (43% of Romania's active population) held loans with banks and/or the NBFIs, which represents a decrease of 6% in the number of indebted consumers from 2009.

Based on the ECRI data, it may be concluded that the total credit in euros to households per capita doubled in 2011 compared to 1996, while loans in the national currency have increased from 0.034 in 1996 to 4.869 in 2011. At the same time, according to the 2012 Annual Report of the NBR, in 2011 the volume of loans decreased in both cases with 4.5%.[15]

The results for 2012 (until June), based on the data provided by the Financial Stability Report of 2013, and Monthly Bulletins, are the following: 1) the number of persons indebted to the banks and NBFIs was 4.35 million, representing 43% of the active population; 2) the amount of borrowing from banks and NBFIs (including outsourced credits) was 116.5 billion (up from USD 115.2 billion in December 2010).

a. *How many consumers have mortgage debt?*[16]

b. *How many consumers have motor vehicle debt?*

c. *How many consumers have other debt (credit card, general consumption)?*

Table no.2

Year	Number of consumers with mortgages	Number of consumers with credits for consumption[17]
2008	154,896	4,079,781
2009	168,457	4,001,816
2010	191,144	3,848,199
2011	213,299	3,696,407
2012	256,108	3,695,149
2013	261,960	3,542,118

Source NBR (reply to questionnaire, 26 February 2014)

12 NBR Report Financial Stability, 2007, p. 69.

13 According to NBR calculations, see Chart 5.2.9 Developments in households' debt service and household loans as a share of the annual disposable income, available at Question 8.5 of the present Study.

14 In June 2011, the non-performing loans (hereinafter NPL) ratio generated by this segment in the banking sector was 15.8% versus 7.9% for the entire household sector. See NBR Financial Instability Report of 2011, p.102.

15 2012 Annual Report, NBR, p. 23.

16 See Chart 3 Changes in Households Credit Standards, Chart 3.2.6 Development of consumer credit Ron mill, and Chart 3.2.7 Development of mortgage and real-estate loans Ron mill. of the Financial Stability Report of the NBR from 2006.

17 A consumption credit is a credit taken by a consumer for consumption purposes and it is not guaranteed with a mortgage. It includes loans to purchase a car/vehicle. The latter cannot be separately identified in the databases available to NBR.

According to a survey conducted by the Euromonitor International Consumer Lending, in the period 2008-2011, card lending and education loans performed best. Current gross lending for such loans increased by 7% and 4% respectively in 2011, compared to only 2% for mortgages. Card lending also increased, due to the fact that consumers became more accustomed to using their cards for daily expenses and paying monthly bills.[18]

d. What percentage of those "indebted" consumers / households (a, b, c) is:

i. Single / married

Proportion of those in households with outstanding debts of over 100% of household

disposable income by marital status (% of each group): Never married: 1.8%; married: 1.2%; separated/divorced: 3.3%; widow: 0.9% (data provided by EU-SILC 2008)[19]

ii. With / without children?

According to EU-SILC 2008 data, the proportion of those in different types of households with outstanding debts of over 100% of household disposable income (% of each group) depending on the number of children in the household was: households with no child -1.3 %, with one child-1.0%, two children -1,6%, more than three children - 4.2%; household living alone: 1.3%, Single parent: 7.3%, other 1.4%.[20]

iii. With / without work?

No data available.

iv. Retired?

No official data available. However, retired persons can only obtain consumer credit, as banks condition credit agreements for the acquisition of property on the requirement that the loan is paid by the time the debtor reaches 65 years old.[21]

v. Low-income consumers?

No data available.

2. How many consumers are considered "over-indebted" in the country? (since 2000)

The lack of an official definition of over-indebtedness poses a problem in the collection and analysis of data. The National Bank of Romania focuses on overdue payments: In 2006, the NBR noted in its Financial Stability Report that although the volume of overdue payments was on the rise in 2005, the share of overdue payments in total loans granted to households went down in that same year. The overdue payments ratio decreased in 2006, reaching 0.37% in December.[22]

Since 2008 there has been a steady rise in defaults. The risk of default was forecast to increase from 2008 as the general tendency of the population was to contract long term loans, and in foreign currencies (euros, Swiss francs and US dollars) in spite of the fact that income was earned in the national currency. Most of the credit generating over-indebtedness was contracted in 2007-2011, with the above mentioned characteristics. The fact that at the beginning of this period the rules on creditworthiness of debtors required by lenders were very loose could have been a cause of why credit contracted in that period generated such high levels of over-indebtedness.

18 http://www. EURmonitor.com/medialibrary/pdf/samples/sample_report_consumer_finance_consumer_lending.pdf

19 Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, p. 38.

20 Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, p. 36-7.

21 Interviews with debtors and representatives of banks.

22 2007 Financial Stability Report, NBR.

Overdue payments ratio doubled in 2008, reaching 1.42% in February 2009. The sharp deterioration began in the first semester of 2008. At the end of the year, the number of overdue payments tripled, while the growth rate of loans to households decreased markedly. Overdue payments for loans granted in foreign currencies accounted for one third of the total (from 18.3% in February 2008), as the depreciation of RON had an adverse impact on the debt service capacity.

In 2009, overdue payments were equally significant, as they accounted for 12.2% of total credit (March 2009), which, according to the NBR Annual Report for 2009, could be indicative of an uptrend in overdue payments ratio.

The rate of non-performing loans has increased from 11.7% of total loans in September 2010 to 14.2% in September 2011, for all types of credit.[23]

The 2011 Annual Report issued by the NBR noted that the non-performing loan rose in the case of households: up to 8.2% at the end of December 2011 and 9.0% at the end of March 2012.[24]

A study commissioned by the European Commission shows that in 2011 more than three in ten households were in arrears.[25]

The pressure resulting from the exchange rate and deterioration of the financial situation of debtors led to an increase in non-performing loans[26], which rose in September 2013 to 21.56%. This is three times higher than at the end of 2009, when the rate loans whose maturities exceeded at least 90 days was 6.46%.

According to a survey by the European Commission, in terms of the number of affected households, Romanian households' over-indebtedness is higher than the EU average.[27] It was reported that more than 30% of households in Romania were over-indebted in 2011.

a. How many individual consumers / households are behind with the repayment of (up to 3 months and more than 3 months):[28]

i. General consumption loans

Please see Table no. 4 for precise numbers.

ii. Motor vehicle loans

No data available.

23 Short study published by the Financial Companies Association of 17.11.2011.

24 See 2011 Annual Report NBR, p.38, report publicly available at http://www.bnro.ro/Regular-publications-2504.aspx

25The over-indebtedness of European households: updated mapping of the situation, nature and causes, effects and initiatives for alleviating its impact, study conducted in January 2013 by Civic Consulting of the Consumer Policy Evaluation Consortium for the European Commission, available online at http://www.bristol.ac.uk/geography/research/pfrc/news/pfrc1301.pdf

26 The present Study uses the notion of non-performing loans (NPLs) as defined by the NBR which includes both the loss and doubtful payment overdue loans. Therefore, in addition to the 90 days+ overdue loan rule, corresponding to the weakest credit quality category ("loss"), the NBR includes in the NPLs also the second-weakest category ("doubtful"), which are those loans overdue for less than 90 days but where due to the deterioration of legal proceedings of the debtor or because legal proceedings have been initiated in view of recovering claims, there are high chances they will exceed the 30 days limit. See S. Barisitz, Non-performing Loans in CESEE An Even Deeper Definitional Comparison. However NBR recommends the definition of NPLs as the 90 days+ overdue loan for reports and international comparison R. Popa, Non-performing Loans Methodologies and Comparisons, Financial Stability Department, NBR, p.19.

27 The over-indebtedness of European households: updated mapping of the situation, nature and causes, effects and initiatives for alleviating its impact, study conducted in January 2013 by Civic Consulting of the Consumer Policy Evaluation Consortium for the European Commission.

28 See in the NBR Monthly Bulletin 7/2005m Chart 3.2.13 Payment overdue from bank credits to households Ron Mill for the period January 2000 – July 2005

iii. Student loans

No data available.

iv. Credit card debt

In 2008, the proportion of people in households with outstanding balances on credit cards (% of total): total 0.8; over 33% (of annual income) was 0.2 % of total; over 100% (of annual income) - 0.1 % of total.[29] While we cannot provide figures for post 2008, a recent survey found that credit card debt is the leader in terms of defaults.[30]

v. Mortgages / housing loans

Please see Table Nos. 3 and 4 for precise numbers.

vi. Interests

The share of the debt service in households' monthly gross income is relatively high in Romania compared to other EU countries.[31] A significant determinant of this has been the interest rate spread between loans in domestic currency and those in euros that has recently seen a significant decline. Another contributing factor to the higher interest rate spread has also been the large share of consumer loans in total loans to households (54% in Romania, compared to 27% in the euro area, in June 2013), considering the generally higher interest rates on consumer loans than those on real-estate loans. Where the interest rate influence is not taken into account and indebtedness is calculated only based on the debt in stock (the principal), the levels of indebtedness in Romania become comparable or even lower than those in the euro area (for example, the share of bank loans to households in GDP was 17.2%, compared to a 55.1% average in the euro area, in June 2013).

b. How many individual consumers / households have initiated bankruptcy proceedings?

Bankruptcy proceedings for natural persons are not available in Romania.

c. How high is the average amount of outstanding debt?

Table no.3

Year	Number of over-indebted consumers (all credits)[32]	Number of over-indebted consumers with mortgages	Number of over-indebted consumers with credit for consumption	Amount of the outstanding debt for mortgages (RON)	Amount of the outstanding debt for credits for consumption (RON)
2008	239,511	1,352	219,140	134,278	4,540
2009	408,020	2,936	363,883	227,377	4,952
2010	431,526	4,252	382,511	243,173	4,400
2011	390,379	5,086	343,632	275,516	3,489
2012	434,151	7,009	384,609	312,849	2,894
2013	379,415	7,774	332,869	287,632	4,308

Source NBR (reply to questionnaire, 26 February 2014)

29 Source: EU-SILC 2008, 'Total' refers to all in the category; 'Over 30%' and 'Over 100%' refer to the amounts relative to annual income. See for more details Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, p.28.

30 Euromonitor International Consumer Lending in Romania.

31 See further Chart 5.14 Households' indebtedness-aggregate indicators and Chart 5.15 Households' indebtedness – EU comparisons (median values) in the 2013 NBR Financial Stability.

32 By over-indebted consumers we refer to those consumers that are behind payment for more than 90 days.

d. What percentage of those "over-indebted" consumers / households (a and b)is:

i. Single / married

No data available

ii. With / without children?

More children generally coincides with there being a greater chance of becoming over-indebted for low income households.[33]

iii. With / without work?

According to EU-SILC 2008, the proportion of those in households with outstanding debts of over 100% of disposable income by work intensity (percentage of each group) is: 0-0.19: 2.9%; 0.20-0.50: 2.2%; 0.51-0.74:1.1% 0.75-1.0:1.0%.[34]

Adverse developments in the labour market and looser conditions under which loans had been granted are the main causes that affected the population's ability to pay its debts to financial institutions. Consequently, the NPL ratio increased moderately during the period December 2009 - June 2011 (1.5 percentage points), reaching 7.9%.[35]

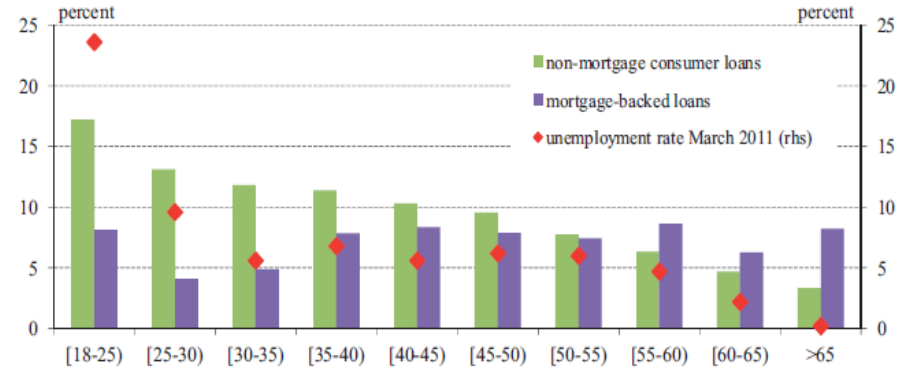
iv. Retired?

Data for 2007 - Total: 1.5; Age 0-15: 2.3% of this group; 16-24:1.6% of this group; 25-39:1.2% of this group; 40-64: 1.8% of this group; over 65: 0.6% of this group; household with all adults age 25-39:1.2% of this group; 40-64: 1.6% of this group; over 65: 0.4% of this group.[36]

See the answer at II.4.d.iv.

Table no.4

Chart 5.20. NPL ratio by age group and by loan type (June 2011)



Source: NIS, CCR, Credit Bureau, NBR calculations

v. Low-income consumers?

33 NBR Financial Stability Report 2011.

34 Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, p. 41.

35 The NBR Financial Stability Report of 2011, p. 111.

36 Table 10 Proportion of those in broad age groups with outstanding debts of over 100% of households' disposable income (percentage of each group). Source: EU-SILC 2008.

In 2008, those who had outstanding debts and/or arrears of over 100% of disposable income were 1.7% of the total, 1.1% of those with income above 60% median, 3.1% of those with income below 60% median, and 2.7% of the materially deprived.[37]

Roughly 85% of loans were granted to individuals with a monthly income below RON 2,000 (approximately €350) in 2009. These are also the loans generating the most overdue payments. In 2009 overdue payments were largely accounted for by debtors with an income of up to 1,500 RON (61% of overdue amounts and 80% of the number of overdue loans), which heightened the risks. Moreover, the ratio of overdue payments for debtors with an income below RON 500 (approximately €110) was about five times higher than those receiving the average income. In spite of the low level of household indebtedness compared to other EU countries, it was acknowledged that Romania was among the group of countries with the greatest repayment problems. On average every fourth household declared arrears in repaying at least one loan.[38]

In 2012, the population with income below 700 RON (approximately €150) per month had the highest level of underperforming loans, with rates of 25% to 11% in consumer and mortgage credits. The NBR analysts calculated that the NPLs of the consumers with a monthly net income of more than 700 RON amounted to 2.5 billion RON, which means that from the total number of households, this segment of the population had outstanding loans of 4.1 billion RON, the equivalent of approximately 40% of total non-performing credits of the population.

In case of consumers with a net income between 700 and 1,500 RON per month, instalments due for over 90 days amounted to between 1.5 and 1.6 billion, which amounted to a total of 2.5 billion of overdue payments. The two categories represented almost 70% of the population of non-performing loans.[39]

According to the NBR Report of 2013, in Romania, borrowers with low incomes hold a relatively significant share of the banks' portfolio. Borrowers with net incomes below the economy-wide minimum wage posted the highest indebtedness (62%, compared to 37% economy wide, median values, in June 2013), and the highest asymmetry of indebtedness, with a more pronounced deterioration trend compared to higher income earners:

"Low income earners are generally the most exposed to face problems in timely repaying their financial obligations. In the case of both consumer loans and mortgage loans, the indebtedness of non-performing borrowers with monthly net incomes below the economy-wide average is higher than that of total non-performing borrowers. This higher indebtedness is tightly correlated with a higher non-performing loan ratio of below-average income earners."[40]

III. Numbers on evictions

1. How many evictions have there been per year since 2000 (or later if earlier data not available)?

In order to manage the credit risk, banks resorted in 2012 and at the beginning of 2013 to a set of measures to clean their balance sheets and manage non-performing assets. One of the solutions most

37 Table 9 Proportion living in households with outstanding debts and/or arrears of over 100% of disposable income for different categories of household (percentage of each group). Outstanding debts are the sum of overdrawn bank accounts, outstanding credit card, balances and arrears on other credits or loans and on housing and other bills. Materially deprived is defined as not being able to afford at least three of nine specified items. See for more details Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, p. 32.

38 P. Anioła &Z. Gołaś, Differences in the Level and Structure of Household Indebtedness in the EU Countries, Journal of Contemporary Economics, (2012), Vol. 6, Issue 1, pp. 46 – 59.

39 In addition to the NBR Financial Report of 2013 , see also http://www.business-adviser.ro/bnr-romanii-sunt-printre-cei-mai-indatorati-dintre- Europeni.html

40 See Financial Stability Report of the NBR of 2013, p.130.

employed by banks was the initiation of foreclosure, applied to approximately 60% of the volume of non-performing loans (more specifically, in May 2013 the share stood at 30% for consumer loans without collateral and more than 55% for mortgage-backed loans). Moreover, there are signals that the recovery rate of non-performing loans is higher in case of foreclosure with seizure of assets (compared to foreclosure without seizure of assets), but the former solution is implemented by a small number of banks,[41] which is motivated by credit institutions in view of the further uncertain prospects for the real-estate market. With regards to the assignments of non-performing assets, banks anticipate that in the second semester of 2013 more than 70% of the forecasted assignments will relate to non-mortgage-backed consumer loans.[42]

2. Who are the persons affected (percentage of young people, families, old people, unemployed)?

Most affected persons are, according to aforementioned data and the data provided under X.1, the unemployed and those with income below 1,500 RON (approximately €310), and the unemployed or young people with families.[43]

Relevant legal framework

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

1. Is the CCD 2008/48 implemented into national law?

Directive 2008/48/EC was transposed into the Romanian legal system on 21 June 2010 when the provisions of Government Emergency Ordinance No. 50/2010 (OUG 50/2010) on credit agreements for consumers entered into force.[44]

2. Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?

Under its recognised margin of discretion, Romania decided to choose an implementation of the Directive on consumer credit agreements that extended the required substantive and temporal scope of the EU Directive. The transposing act (OUG 50/2010) contained some important differences when compared with the Directive, which are, by reference to the question, the following:

- It modified the temporal scope of the Directive, stating that its provisions apply to ongoing credit agreements, including those concluded before the date of its entry into force, and not only to future agreements as provided by the Directive (Article 95 of OUG 50/2010); this specific norm has been the subject of significant litigation. Both its constitutionality and its compatibility with Directive 2008/48 and several provisions of the TFEU were challenged by one bank in particular within the framework of proceedings for the annulment of sanctions applied by the National Authority for Consumers Protection (NACP). During this litigation, which included a reference to the CJEU[45] and only four months after the entry into force of OUG 50/2010, Article 95 of this act

41 Out of the 32 banks participating in a Questionnaire on Loan Portfolio Management Techniques (May 2013) distributed by the NBR, only a few declared their option for such a measure: five banks in the case of mortgage-backed consumer loans and eight banks in the case of real-estate loans.

42 Financial Stability Report of the NBR of 2013, p. 107.

43 Based on interviews with consumers, and financial reports of the NBR and NIS.

44 Published in the Official Journal, Part I, No. 389 of 11.06.2010, 10 days from its publication in the Official Journal, the GEO entered into force.

45 Case C-602/10 *SC Volksbank România SA v Autoritatea Naţională pentru Protecţia Consumatorilor – Comisariatul Judeţean pentru Protecţia Consumatorilor Călăraşi (Volksbank)*, judgment of the CJEU of 12 July 2012.

was reversed, in the sense that it was amended to the effect that the OUG was no longer to be applied to on-going agreements, but only for the future. (see section XIV.1.b)

- It extended the material scope of the Directive, making it applicable also to credit secured by mortgages or by other rights on immovable property (Article 2 of OUG 50/2010); this too was challenged by the same credit institution mentioned above.
- It introduced a series of detailed conditions on information duties binding the creditor, which go beyond those required by the Directive and which also apply to credit secured by mortgages or by other rights in immovable property, concerning: the deadline for presenting pre-contractual information; a very precise and detailed format of the credit agreement; detailed obligation of warning the consumers on the consequences of missing payments;[46] added information duties applicable to credits secured by mortgages;[47] a concrete time limit binding the creditor within which the latter has to inform the consumer of the decision to enter or not into the credit agreement; the payment of instalments.

3. With regard to the Mortgage Credit Directive Proposal: will there have to be an adjustment of national law if the Proposal is adopted as it is? What would be the changes in particular?

Several provisions mentioned by the Mortgage Credit Directive (MCD) proposal on assessing the creditworthiness do not have an equivalent in the OUG 50/2010, for example, Articles 10(2), 14(1), (4), 22, and 29. OUG 50/2010 do not contain detailed provisions on the creditworthiness of the consumer, as required under the MCD. With the entry into force of the MCD, lending institutions will have to take into consideration the debtor's current financial situation but they will also have to consider its evolution and the possible difficulties they may encounter in repaying the loan. Similar rules on customer creditworthiness assessments, and the recommendation to take into consideration hazards that may occur during the life of the loan were provided by the NBR in its Regulations from 2011 and 2012.

In December 2011, the NBR delivered its opinion on a proposal for a law regulating mortgage-backed loan agreements. The proposal is still under discussion in Parliament. The MCD would allow the conversion of the mortgage secured loan's currency in RON at the rate of the day on which the application is submitted. Currently, Romanian consumers do not have this possibility, they only have the possibility of refinancing the mortgage secured loan, if they want to continue to pay the credit from a foreign currency using the national currency. This refinanced credit is treated by the bank as a new credit. The main disadvantage of refinancing is that borrowers must provide additional collateral for the loan because the value of the mortgaged properties has dropped sharply in recent years.[48]

4. How is the national legal framework with regard to the UCT 93/13?

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46 According to Art. 5(m) of the Directive, one of the duties of the creditor to inform the consumer before signing the credit agreement refers to "the warning regarding the consequences of missing payments"; Art. 14 (o) of OUG 50/2010 as amended by OUG 50/2010, adds to this provision a more concrete obligation based on information required under section 3 cost of the credit of Annex Ii Standard European Consumer Credit Information: "Warning must, necessarily, contain the time limit when reporting to the credit bureau is done and the minimum amount at which the creditor can trigger the foreclosure proceedings."

47 OUG 50/2010 includes a specific provision on mortgage credit under the provision on 'pre-contractual information', which reads as it follows: "In the case of credit secured by a mortgage with another security comparable to or rights in immovable property, as well as contracts purpose of which is to acquire or retain property rights relating to an existing or projected building or renovating, planning, consolidation, rehabilitation, expansion or increase in value of a property, in addition to the information provided in par. (1), the creditor shall inform the consumer that they can return it in pre-contractual stage, only the following expenses, where applicable: a) expenditure loan application preparation, b) Estimated cost for the mortgage and related securities."

48 According to a statement made by the director of the supervisory department of the NBR, during a Conference in Bucharest in late 2013, the problem of refinancing of foreign currency credits in RON exists mainly in regard to those loans contracted in Swiss Francs, during 2007-2008, since the debtors do not have guarantees to cover the loan in case of refinancing. „Their value is half the credit balance."

Law no. 193/2000 regarding unfair terms in contracts[49] implemented Directive 93/13/EEC and is *lex specialis* in relation to the contract law laid down by the Civil Code. In its turn, Law 193/2000 is applied as *lex generalis* in relation to OUG 50/2010.

V. Enforcement of consumer credit contracts

1. What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?

If the debtor exceeds the monthly payment deadline (30 days), the person is registered by the bank/financial institution with the Credit Bureau and/or Central Credit Risk, and will have to pay penalties. According to Article 1516 of the Civil Code, the creditor has a choice between proceeding to the enforcement of the obligation or terminating the agreement.

In principle, the creditor can ask for the forced sale of the mortgaged property even after the first overdue instalment, according to the general provisions of the Code of Civil Procedure, Book V. The request of the creditor is submitted to an enforcement officer who will then lodge a request for an enforcement order before a court. Once approved by the court in chambers without the notification of the parties, the enforcement officer can proceed to the execution of the order for payment of the credit and the sale of the mortgaged property. However, even if not expressly provided by legal norms, the common practice is that, before having recourse to court enforcement, the bank or a third party to which the bank has transferred its credit will, together with the debtor, search for a solution that will ensure repayment. However, the bank/financial institution has no obligation to resort first to re-organisation measures.

Usually loan agreements contain a standard clause which entitles the parties to terminate the contract if the other party does not fulfil its obligations under the contract.[50]

2. What are the requirements to initiate enforcement procedures against the consumer?

In order to initiate the enforcement procedure, a creditor must hold a writ of execution (in Romanian 'titlu executoriu'). According to Article 662 of the Code of Civil Procedure the only necessary condition is to be in the possession of a debt that is certain, of a fixed amount and immediately payable.[51] The debt becomes certain, of a fixed amount and immediately payable once the consumer has exceeded his first month payment of instalments, although in practice it is commonly required that more than 90 days passed after the consumer was not able to pay. There is a possibility whereby the creditor may declare the loan due in advance if the consumer has not met its obligations under other contracts with other creditors.[52]

It very often happens that the lender bank/financial institution assigns its rights over the credit to a third party, usually a private institution which will directly handle the restructuring and recovery of the amount of the credit from the individual debtor.

3. What are the steps of such enforcement procedure?

There are three types of enforcement procedure, regulated by the Code of Civil Procedure:

49 The Law 193/2000 on unfair terms in contracts concluded between professionals and consumers published in the Official Journal of Romania, Part I, no. 506, 10.11.2000, last amended by Government Emergency Ordinance no. 4/2013, Official Journal of Romania, Part I, no. 68, 31.01.2013.

50 Based on interviews with consumers and lawyers representatives consumers' interests.

51 Definition at Art. 379 (4) Code of Civil Procedure. Therefore the credit agreement must have clearly stated the underlying debt, and the payment obligations are due and payable at the moment of initiating the enforcement.

52 As provided by Art. 24 of OUG 50/2010.

- Enforcement over real estate; Enforcement over movable assets; Enforcement over wages, accounts or other income.
- Recent amendments of the Code of Civil Procedure, dating from 2013, aim at the simplification of the enforcement procedure and shortening of the duration of proceedings.
- The procedure, regardless of its type, always starts with the request of the creditor for an enforcement of obligations arising from the contract lodged with a bailiff.

Where the debtor does not pay at the request of the bailiff, the latter will lodge a request for an enforcement order with the competent court within three days from the moment the creditor submitted his request to the bailiff (Article 818). The court proceedings are non-contentious. According to the new provisions, the court is bound to take a decision within seven days from the moment when the claim was filed by the enforcement officer and must write the order in a maximum time limit of a further seven days.[53]

The order of the court granting the request is final. The order dismissing the request may be appealed within five days and only by the creditor.

The debtor will be informed about the duty to pay the credit immediately or within the legally required period and will be notified about the consequences of non-payment, namely that the court order court will be enforced against them. In the case of mortgaged properties the debtor has fifteen days from the moment the order of the court is notified to him. In case the debtor fails to pay within this fifteen day period the bailiff will start the evaluation procedure of the immovable property. From this moment on, the debtor may lodge various objections and claims regarding the way the enforcement order is carried out by means of a special procedure called "objection to enforcement", which we will detail in section 4.a below.

The next step is the advertisement of the enforcement followed by the evaluation of the mortgaged property, which is mandatory and may be challenged by the debtor during the special procedure of objection to enforcement.

The sale at public auction follows next, which may include several stages. With every subsequent auction, the value of the forced sold property decreases.

4. Can the consumer raise substantive objections against enforcement?

a. Which ones?

b. What is the legal effect of such objections?

According to the new Code of Civil Procedure, the consumer can raise objections against the enforcement order within the special procedure called 'objection to enforcement' (*contestatie la executare*).

The type of grounds the debtor can raise to object to enforcement depends on a very important distinction between two situations: when enforcement is carried out pursuant to a final court judgment, and when it is carried out on the basis of an act other than a court judgment, such as a contract that has not been challenged in court before. This distinction is important because in the first situation (enforcement pursuant to a court judgment), considering that a court judgment is *res judicata*, if the issue of the potential unfairness of a contractual term has not been raised during the proceedings that ended with the judgment, the objection to enforcement may regard only new aspects that appear during the enforcement proceedings.

53 These deadlines were not expressly provided by the former Code of Civil Procedure, which led to divergent jurisprudence on the length of proceedings.

In the second situation (non-judicial act), if the creditor initiates enforcement proceedings based directly on the contract and there was no previous litigation where the potential unfairness of a contractual term could have been raised, the objection to enforcement may also regard this aspect, and not only new issues that appear during the enforcement proceedings.

During the objection to enforcement, the debtor or the creditor may ask the court to stay the enforcement proceedings.

According to Article 718(1) of the Code of Civil Procedure, the court has the power to stay the enforcement proceedings for 'reasonable grounds'. Due to the general wording of the provision it can be argued that the discretion conferred to the judge may lead to a stay of proceedings in a situation where the debtor introduces a plea that the contract includes an unfair term and which had not been brought before. This would be possible in the second situation described above, where there were no previous judicial proceedings disputing the legality of the contract.

However, while the court enjoys discretion regarding the evaluation of the grounds for ordering a stay of enforcement proceedings, the mandatory condition laid down at paragraph (2) of the same article may raise problems. According to this paragraph, the person who asks for a suspension of the enforcement proceedings must lodge a deposit in an amount that varies according to the value of that which is in dispute in the objection to enforcement proceedings.[54]

The possibility under paragraph (4) of the same Article to order immediately a stay of enforcement proceedings as a matter of urgency, is still made subject to the same condition of lodging a deposit calculated as mentioned above.

As to the effects of the objection to enforcement, if the debtor is successful and the court finds that the object of enforcement is laid down by an unfair term of the contract, the court will revise or annul the contract (as the act which is at the base of the enforcement proceedings). If the objection to enforcement is unsuccessful, the person who initiated it (in our case the debtor) may be ordered to pay damages caused by the delay in enforcement and even an administrative fine if bad faith is proven.

5. *Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?*

Yes. In theory, the Civil Code allows for the adjustment of contractual terms for "hardship" ("impreviziune"), but the conditions are so restrictive that it is hardly applicable: the change in circumstances must have occurred after the agreement was concluded; the change in circumstances and its extent were not and could not have been reasonably foreseen by the debtor when the agreement was concluded; the debtor did not accept the risk of the change in circumstances and it could not have been reasonably considered to have accepted it; the debtor tried in a reasonable time limit and in good faith to negotiate the reasonable and equitable adjustment of the agreement.

a. *How is the term "unforeseen/unforeseeable events" defined?*

According to Article 1271 of the Civil Code, entitled "Hardship" ("impreviziunea"), the parties to a contract must fulfil the terms of the contract, even if performance of the contract becomes more onerous or the remuneration decreases in value. However, the same Article provides for the situation when the performance of the contract may become "excessively onerous due to an exceptional change in the circumstances which would render the obligation of the debtor to perform the contract manifestly unjust".

b. *If adjustment is possible, what are its legal effects?*

54 10% for a value under 10,000 RON; 1,000 RON plus 5% for anything over 10,000 RON; 5,500 RON plus 1% for anything over 100,000 RON; 14,500 RON plus 0.1% for anything over 1,000,000 RON.

The legal effects would be "the equitable distribution between the parties of losses and gains which result from the change in circumstances".

6. *Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?*[55]

As to the definition of Hardship, please see the answers at 5.a and b.

VI. National legal framework applicable for over-indebtedness

1. *What are the possibilities for consumers in case they are considered "over-indebted"?*

Especially since 2009, in the case of borrowers experiencing financial difficulties, credit institutions make use of refinancing and restructuring of instalments. For extreme situations, the lender may offer a grace period for a total number of months during which payments are temporarily suspended. The unpaid instalments will cumulate in the loan balance to which further interest is added, leading to increasing debt.

Any amendment to the credit agreement, including loan restructuring, are commonly charged with a single fee for the service offered to the consumer, whose value can vary significantly from one financial institution to another.[56]

According to the Financial Stability Report of the NBR of 2013, loan rescheduling is one of the most used restructuring methods. However, it has not proved very efficient in improving borrowers' repayment behaviour. For both households and non-financial corporations, the rate of recovery of the rescheduled loans[57] is lower than the recovery rate of the loans for which no contractual changes were made. Moreover, rescheduling does not lead to a significant improvement in non-performing loans either, as recovery rates are relatively similar. It also appears to be driven by the credit institutions' concern to reduce additional provisioning requirements.

a. *Is there the possibility for the consumer to reorganise debt or obtain debt relief?*

Romania has one of the most restrictive laws on the treatment of over-indebtedness of individuals, according to a study written by London Economics (LE) for Financial Services User Group (FSUG).[58] Unlike most EU countries, Romania has no legislation in place that offers the opportunity to individuals – as opposed to legal persons – to declare personal bankruptcy and get obtain relief or discharge in a situation where they can no longer afford to pay the whole debt. When consumers are in a situation where they can no longer fulfil their payment obligations towards banks or financial institutions, the only solution is reorganisation of debt. When that fails, legal proceedings for the seizure of the movable or immovable property and selling at auction follows. Reorganisation of debt and eviction are often conducted by third parties, to whom the bank or financial institution assigned the credit agreement.[59] Although the level of effective restructuring of loans is low, according to

55 If by „frustration" we mean a situation that occurs without default of the contractual parties and which render the contractual obligation incapable of being performed, then the Civil Code provision on „Hardship" is the closest to this definition.

56 For example, CEC Bank charges no fee, BCR charges 10 EURs, ING Bank - 500 RON, OT Bank - 150 RON, BRD - 50 EURs, Emporiki Bank – 40 EURs (figures from 2010).

57 Those loans with a payment delay of between 1 and 90 days.

58 http://ec. EURpa.eu/internal_market/finservices-retail/docs/fsug/papers/debt_solutions_report_en.pdf

59 Information confirmed by a study on the means to protect consumers in financial difficulty: Personal bankruptcy, *datio in solutum* of mortgages, and restrictions on debt collection, abusive practices, see http://www.economica.net/studiu-london-economics-faliment-personal-supraindatorare-anulare-datorie_51181.html; and interview with judge hearing cases of evictions and enforcement of debts.

financial stability reports issued by the NBR, banks seem to favour this approach instead of having recourse directly to enforcement procedures before courts.

The reorganisation of the debt is done by the lender in agreement with the debtor while respecting the general rules on the prohibition of unfair clauses in relation to consumers and the general regulation of the NBR. The Romanian Banking Association (RBA) reported that there are three possibilities to address over-indebtedness: refinancing, rescheduling, and restructuring. From a lender's perspective, the most successful process is rescheduling, followed by restructuring.[60]

There are several ways used by banks to reorganise debt:[61]

- Postponement of payment; this method is applicable in the case of short-term difficulties (one-three months).
- Extension of the duration of the credit agreement, if the credit limit is already set up or the agreement is concluded for a duration exceeding fifteen-twenty years (such as mortgage credit), this option is usually not possible An important aspect is the consumer's age, which cannot (usually) exceed 65 years at the end of the duration of the credit agreement. Further, a longer period for repayment of the loan means a higher total cost.
- Reducing the monthly instalments for short periods (e.g. six months): for temporary problems, this method entails a temporary reduction of the additional costs of the credit in view of reducing the instalment. This method does not need an extension of the duration of the loan. After financial recovery, the consumer returns to the normal rates.
- Consolidation: consolidation of multiple credits into one, possibly securing them with a mortgage (on the home), which could provide a longer repayment duration and lower rates.
- Guarantor: finding a guarantor who can help to pay the instalments.
- Advance payment: agreeing with the bank conditions of advanced payment, when a certain large amount will be collected and available to pay the debt (credit).

i. How are the terms reorganisation and debt relief defined?

The law does not contain definitions of the terms "re-organisation" and "relief". Romania does not have personal bankruptcy legislation.

ii. What are the requirements for re-organization and relief?

See i.

iii. How many consumers have obtained from re-organisation or debt discharge?

The share of restructured loans to households and non-financial corporations in the loan stock reached 9.6% in September 2010, up from 6.6% in December 2009. According to the information supplied by credit institutions, non-financial corporations (66% of all restructured loans) were the first to obtain restructuring of debt, and households were next (almost 34% of the total figure).[62]

According to a survey conducted by the NBR in May 2013, the share of restructured loans[63] in the total exposure to the population stands at 10.7%, with a preponderance of foreign currency loans (81% of all restructured loans).

60 Study on means to protect consumers in financial difficulty: Personal bankruptcy, datio in solutum of mortgages, and restrictions on debt collection abusive practices Final Report, prepared by London School of Economics, December 2012, available online at http://ec. EURpa.eu/internal_market/finservices-retail/docs/fsug/papers/debt_solutions_report_en.pdf

61 Based on consultation of the websites of several major banks: Reiffeisen Bank, BCR, Volksbank, ING Bank, Unicredit.

62 Financial Stability Report of the NBR of 2013, p. 107.

63 Out of the total of the population to whom restructured loans had been granted, 69% had delays in payment of less than 90 days.

b. Is there a possibility for consumers to attain discharge of debt (Restschuldbefreiung)?

There is no specific legislation or private regulation for the financial sector allowing debt discharge. In the framework of the general rules of contract law, Article 1629 of the Civil Code only regulates "Remiterea de datorie", which corresponds to the term "discharge of debt". According to a survey conducted by the NBR in May 2013, many banks alleged they had practiced debt cancellation operations in order to manage the loan portfolio. The volume of these operations is, however, modest.

i. How is discharge[64] *defined in the national context? (Is there a definition?)*

Article 1629 of the Civil Code defines "remiterea de datorie" as the possibility a creditor has to free his debtor of his obligations, in total or in part, with or without compensation and it requires the consent of both creditor and debtor.

ii. If discharge is possible, after how many months/years is it possible?

No discharge is possible. In the case of remission of debt, there are no time limits.

iii. If discharge is possible, what are the requirements for discharge?

No discharge is possible. In the case of remission of debt, Article 1629 of the Civil Code does not provide for specific requirements.

c. What are the requirements for initiating bankruptcy proceedings for consumers?

Romania does not have legislation on personal bankruptcy. There have been several attempts to legislate, with the first initiative being taken in 2010. The basic content of the proposal was that a debtor in good faith who files for personal bankruptcy may be fully or partially discharged of debt, after a process of asset liquidation and the completion of a payment plan. The proposal was that, if the debtor, through the payment plan, can repay a minimum of 75% of the debt, then he would be discharged of the remainder and the procedure would be closed, with all the legal consequences of the insolvency erased from all public records and advertisement registers, thereby offering a discharge of 25% of the loan principally owed by the bankrupt debtor.

The banking sector has not supported this proposal, neither then, in 2010, nor recently when discussion on a personal bankruptcy law reopened. A second legislative attempt was proposed by a single deputy, but was also rejected by the Senate, and subsequently rejected in October 2012 by the Government.[65]

The adoption of the law on the bankruptcy of individuals has been postponed without a concrete date, therefore the possibility of initiating bankruptcy proceedings for consumers is not possible.

d. How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?

e. Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can have recourse to? Please list and elaborate on requirements, legal consequences, and numbers of consumers who have gone through the measures in question.

No.

2. Is there a national legal or policy framework for avoiding evictions?

a. Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (i.e. debt relief)?

64 Discharged in this context is understood as release of debt.

65 These reasons were reported in the London Economics Study on means to protect consumers in financial difficulty: Personal bankruptcy, datio in solutum of mortgages, and restrictions on debt collection abusive practices, p. 85.

Yes, the general rule is that the debtor stays in the mortgaged property that is subject to enforcement proceedings. However, during the stage of preliminary formalities for the sale of the property at public auction in the enforcement proceedings, the court may, depending on the circumstances, order the that the property is vacated, in whole or in part, either immediately or in a certain period, at the request of the creditor or the bailiff (Article 829 of the Code of Civil Procedure).

b. Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?

Yes, even after the mortgaged property has been sold at the public auction, and the ownership of the property has been transferred to a third party, Article 895 of the Code of Civil Procedure stipulates that:

> "(1) No evacuation from buildings with housing purposes may be made from 1 December until 1 March of next year, unless the creditor proves that under the provisions of housing legislation, he and his family do not have available adequate housing or that the debtor and his family have another suitable housing where they could move immediately. (2) The provisions of paragraph (1) shall not apply to persons abusively occupying houses, in fact, with no title, or those who have been evicted for threatening life relations or seriously disturbing public peace."

This Article was first provided by the New Code of civil procedure which entered into forced on 1 February 2013.

In the situation covered by the above article, the debtor does not pay rent, as he is not in a contractual relationship with the adjudicator of the house. However, in the absence of any special provision regulating this issue, general rules on damages for loss of use of property may apply.

VII. The regulation of credit bureaus

1. How many credit bureaus are there in the country?

Taking due account of the common internationally accepted terminology, at present, two main types of credit reporting systems exist in Romania: (i) credit registries, which are public entities that are managed by bank supervisory authorities or central banks, and typically collect information from supervised financial institutions, and (ii) credit bureaus, which are privately owned enterprises that tend to cover smaller loans, often collect credit information from bank and non-bank lenders, and provide a range of value-added services, such as credit scores, to bank and non-bank lenders.

In Romania these two types of credit reporting systems are entitled as follows: the Romanian Central Credit Register (CCR); the Private Credit Bureau (CB).

2. Are the credit bureaus public or private?

The CCR is a public entity operated by the National Bank of Romania, of which it is part.

The CB is a private shared private company, which was founded in 2004. On 31 December 2011, the Romanian Office had 36 credit institutions as members, representing approximately 98% of the retail market, together with nineteen non-bank financial institutions.

If there are both public and private credit bureaus:

a. How many credit bureaus are public and how many are private?

One private (CB), while the CCR is part of a public institution, the National Bank of Romania.

b. Do the public and private credit bureaus have different functions and / or procedures? Are they concerned with the same data?

The Credit Bureau (CB) and Centre for Credit Register (CCR) were both created to track the payment behaviour of customers who contracted loans, helping banks to evaluate as accurately as possible the risk of their insolvency. Therefore CB and CCR have similar functions, namely of collecting, storing and handling information on credits contracted on the Romanian market. However, there are important differences in the scope of their functions regarding the subjects from whom they collect data and the range of services.

The Central Credit Register is an institution specialised in the collection, storage and handling of information on the exposure of each declared institution[66] from Romania to those borrowers (both natural and legal persons) who received loans and/or cumulative commitments whose level exceeds the reporting limit (20,000 RON). CCR also handles information on card fraud perpetrated by owners.

The CB collects data regardless of the amount of the loan and only on borrowers who are natural persons.

As to the range of services provided by the two credit reporting systems, the CB, unlike the CCR, provides a range of other services such as quantification of credit risk for the purpose of improving quality of loans, institution of uniform criteria regarding the clients' assessing scoring, banking and financial advice.

3. How are credit bureaus compensated?

The (private) Credit Bureau was established on the basis of the capital paid by the shareholders. The main source of income consists of a monthly fee from the institutions to which it provides risk information (credit institutions and NBFIs) as a price per piece in the case of Credit Reports and scores, or in the form of a monthly fee in the case of alerts).[67]

To provide credit information services, the CCR charges every reporting institution monthly, as it follows:

A fee calculated according to the number of borrowers recorded in the CCR database in the respective month:

- 1,800 RON for reporting institutions with less than 500 borrowers recorded in the CCR database in the respective month and to whom the CCR makes available the "Registered entities' overall risk statement";
- 2,300 RON for reporting institutions with 500-1,000 borrowers recorded in the CCR database in the respective month and to whom the CCR makes available the "Registered entities' overall risk statement";
- 2,500 RON for reporting institutions with more than 1,000 borrowers recorded in the CCR database in the respective month and to whom the CCR makes available the "Registered entities' overall risk statement";

A fee calculated according to the number of queries made with the consent of potential borrowers:

- 100 RON for reporting institutions that made queries in relation to all new borrowers to whom they granted loans in the respective month;
- 200 RON for reporting institutions that made queries in relation to at least 50% of the new borrowers to whom they granted loans in the respective month;

66 Credit institution, non-banking financial institution registered in the Special Register, payment institution that records a significant level of lending or electronic money institution that records a significant level of lending.

67 Information provided via email by the Romanian Banking Association to a questionnaire sent by the authors of the current Report.

- 300 RON for reporting institutions that made queries in relation to up to 50% of the new borrowers to whom they granted loans in the respective month.

4. How do the credit bureaus collect data?

The Credit Bureau collects data from participants on a voluntary basis (Contract of Participation), while the Central Credit Register collects data on a mandatory basis, according to a regulation issued by the NBR. *Regulation No. 2 of 9 January 2012 on the organisation and functioning of the Central Credit Register operated by the National Bank of Romania* provides that reporting institutions shall submit to the CCR, under the terms and conditions set out in the Regulation, the credit risk information on every borrower meeting the reporting requirements (meaning that the reporting institution has incurred an individual risk against the borrower), as well as any card fraud information available. In order to meet this obligation, the reporting institution shall submit credit risk information to the CCR electronically, via the Interbank Communication Network, on a monthly basis, within the reporting period, through the mandatory use of certain procedures specified in the Regulation.

5. In what way do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?

The data collection and processing by credit bureaus is regulated by Decision No.105 of 2007 issued by the Romanian National Authority for the Supervision of Personal Data Processing,[68] which came into force on 27 February 2008. The main provisions applicable to the Credit Bureau are the following:

- participants in the Credit Bureau System can be banks, consumer credit, leasing and insurance companies;
- data storage and their display in credit reports can be done for a period of 4 years from the date of payment of the final instalment of arrears or from the last update provided by the participant.

Moreover, according to Art.24 of Regulation No. 2 of 9 January 2012 on the organisation and functioning of the Central Credit Register operated by the National Bank of Romania, reporting institutions may inquire the CCR database in order to access credit risk information on any individual or non-banking legal entity, subject to the latter's written consent and in compliance with the legal provisions in force. However, the written consent of the registered entity is not necessary if the reporting institution inquires the CCR database in relation to a borrower reported by it during the latest reporting period and/or if the requested information refers to card fraud. Supervision of the credit reporting systems compliance with the aforementioned legal requirements is exercised by the National Authority for the Supervision of Personal Data Processing.[69]

6. What data is collected by credit bureaus?

The Credit Bureau (CB) collects data on borrowers as well as co-debtors and endorsers. Participants in the CB can transmit both positive and negative information regarding payment behaviour of individuals who contracted loans. Negative data about a customer,[70] such as bank arrears, are reported

68 Decision no. 105 of 15 December 2007 regarding the processing of personal data performed in an evidence system of credit bureau type issued by the Romanian National Authority for the Supervision of Personal Data Processing, published in the Official Journal no. 891 from 27 December 2007.

69 The National Authority for the Supervision of Personal Data Processing (NASPDP) supervisory functions are provided by Law no. 677/2001 on protection of individuals with regard to the processing of personal data and on the free movement of such data; while norms on the processing of data are provided by several Decisions issues by the NASPDP.

70 Negative and positive data and information on fraudulent activities or inaccuracies are stored for the duration of four years in the CB system and displayed during this period in the credit report of an individual. However, for those who have applied for a loan and who gave up a credit application or to whom this application has been rejected, information reported to the credit bureau is stored for a maximum of six months from the moment of transfer of this data to the CB system, and it can be accessed by the participants only within this timeframe.

to the credit bureau, only if the delay is more than 30 calendar days and only if the outstanding amount is more than 10 RON (approximately €2). Positive information is transmitted at the termination of the loan contract.

In addition, the CB collects data regarding those individuals with fraudulent activities – those who committed criminal offences or misdemeanours in the banking field so found by a final judgment or a final or uncontested administrative act. Another type of data collected by the CB is data reporting on inaccuracies, i.e. information inconsistencies in the documents submitted on the loan application, due to the fault of the applicant.

The CCR collects data reported by declared persons/entities concerning the identification of debtors owing a sum of minimum 20,000 RON.

The data include:

- information on all loans and commitments of which the debtor benefits: type of loan, maturity, type and value of collateral, debt service, granting date and maturity date, loan currency, amount granted, drawn and undrawn amounts, overdue loans, joint credits/commitments with other borrowers belonging to the same group, loan status, rating grade, probability of default
- information on groups of individuals and/or legal entities including: the group name, group ID, group membership, borrowers who have loans with other borrowers in the group;
- information on card frauds committed by owners: data owner identification card, card type, currency, date of fraud discovery, the amount of fraud.

The CCR database is organized into four files:

- Central file of credit (FCC) contains credit risk information reported by reporting entities, and is updated monthly;
- File overdue (FCR) contains information on credit risk deviations from repayment schedules of up to seven years, and is monthly updated by the Central file credit (FCC);
- File groups (FG) contains information about groups of individuals and/or legal persons who are a group of connected clients/single borrower, and is monthly updated by the FCC;
- File card fraud (FFC) contains information about products card fraud reported by owners reporting entities, and is updated online.

Sharing credit risk information is performed electronically using the Interbank Communication Network.[71]

7. Who are the users of credit bureaus?

The users of the Romanian Credit Bureau are first of all its members, then also other credit institutions and non-banking financial institutions.[72] In addition, private individuals who want to know what data exists on their names can request to receive their credit situation as it is registered at the credit bureau. Information both positive and negative, concerning private persons who have contracted credits and are late with the payments of credit instalments for more than 30 days, is reported and registered at the Credit Bureau. The first request for release of this situation by the Credit Bureau during one year is

71 Dissemination of CRC information to declared persons/entities is done in two ways: 1) monthly reports containing information on all debtors reported that month by the declared person/entity. For each reported debtor, the monthly report contains all available information available at CCR on loans and commitments it has received, without specifying the identity of the creditor institution (overall risk situation); 2) in response to online enquiries (requests for consultation), the declared persons/entities can request two types of information: the overall risk situation and the situation of overdue loans (over seven years).

72 On 31 December 2011, it had 36 credit institutions as members, representing approximately 98% of the retail market, and 19 non-banking financial institutions.

free of charge, while a fee is charged for subsequent requests. The requested information is sent to the individual via post or e-mail within the legal time limit from the registration of the request.

The users of database of CCR are the declared persons/entities and the National Bank of Romania.

(Over-)indebtedness of consumers

VIII. Macro-economic risk factors for over-indebtedness

1. Has there been a housing bubble in the country? Elaborate.

Table no.5

Year	Property Price to Income Ratio	Gross rental Yield City Centre	Gross Rental Yield Outside of City Centre	Price to Rent Ratio City Centre	Price to Rent Ratio Outside of City Centre	Mortgages as a percentage of Income	Affordability
2009	30.29	3.80	3.81	26.32	26.28		
2010	24.28	5.02	4.41	19.92	28.67	333.12	0.30
2011	16.38	4.13	4.22	24.20	23.69	180.83	0.55
2012	15.49	4.10	4.37	24.38	22.90	162.79	0.61
2013	14.33	4.82	4.66	20.74	21.48	143.87	0.70

Source: Numbeo, property investment website[73]

Residential real estate prices rose significantly in 2006 "following the trend of the last four years. The most important urban centres experienced the highest price increase (in Bucharest, a standard flat with no special improvements was almost 53% more expensive than in 2005)."[74]

In 2009, Romania was the country with the highest price for houses per income ratio in the world, though house prices had plunged by 20.62% (-24.22% inflation-adjusted) compared to the previous year.[75] Over the next years, it gradually lost first place: in 2010 it was still among the first 25 countries in the world, in 2011 it was in 27th position, in 2012 in 20th position, and in 2013 in 30th position.

According to the NBR the raising housing prices (in 2007 more than 50% of the average value per square meter of a standard dwelling) were considered to be normal consequences of the economic growth. The NBR held in a Report of 2008 that "the risk of a shock consisting in the steep drop of real estate wealth in Bucharest is low, as the purchasing power is significantly higher and the number of people living or working here remains high."[76] However, the real estate prices have significantly dropped in 2010 and continue to decrease.

2. What is the relation between housing prices and over-indebtedness?

a. How have housing prices developed since 2000 (or later if earlier data not available)?

73 http://www.numbeo.com/property-investment/rankings_by_country.jsp?year=2010

74 NBR Financial Stability Report, 2007, p. 67.

75 More details on the house prices in Romania and their evolution from 2009 onwards, see at http://www.globalpropertyguide.com/ Europe/Romania

76 2008 Financial Stability Report, p. 85.

From April 2003 until December 2003 the average price of a one room apartment doubled reaching €18,000 (the exchange rate between the euro and the US dollar was close): April 2003: 9,000 USD; June 2003: 10,900 USD; August 2003: 15,500 USD; December 2003 18.000 USD. Until 2008, a similar apartment could have been bought to average €80,000.

In 2009, however, the first year of the construction crisis, the Romanian economy suffered a significant setback, of 7.1%, equal of the financial raise registered the previous year. The housing market registered a downward trend strongly with a reduction of 20.6% in twelve months.

In 2010, the financial downturn was more temperate (GDP dropping by 1.3%), but the austerity measures imposed by the Government had a significant effect on the disposable income of Romanians and, consequently, impacted on the price of real estate. This explains the fact that apartment prices continued to drop by 15.6 % on average.

In 2011 the national economy was on an upward trend - thanks to an advance of 1.5% in the GDP, which was translated by a slowdown in the declines registered on the real estate market: over 2011 apartments nationwide were cheaper by about 4% compared to the previous year.

Similarly, in 2012, with a 1 % increase in the GDP, prices by reference to square meters of construction decreased by only 0.5 % from €991 to €986 per square meter.

It is clear that in recent years the downward trend of the economy has had a strong impact on the purchasing power of the population. This is proved the decrease of the amounts borrowed from banks to purchase homes.

In Romania, according to the Bank Lending Survey, residential property prices dropped in the first quarter of 2013 and this trend was expected to continue, according to the EMF Quarterly Review Q1 2013 in the second quarter of 2013. In addition, households' intention to buy or build a home within the next twelve months decreased marginally in the first quarter 2013.[77]

b. How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available)?

See answer to II.5.

3. Has there been an increased access to mortgage credit? In which way? For example: was access to consumer credit facilitated through legislation? And has access to credit become more restricted since the crisis? Elaborate. If possible provide data

During the period between 2000 and 2002, mortgages were granted primarily on the basis of the general law, Law no. 190/1999 on mortgage real estate investment acted as a real incentive to develop this product. The reluctance of banks to grant mortgages under Law no. 190/1999 was due to limitations imposed by its provisions, namely:

- The calculation of the benchmark interest rate on mortgages was to be determined by Government decision, which was not adopted in practice;
- Mortgage loans could be granted only in RON;
- The minimum duration for which mortgages could be granted to households was ten years.

These inconveniences, however, were solved by OUG No. 201/2002 which amended Law no. 190/1999 on mortgages for property investment. Between 30 June 2000 and 31 December 2002, although mortgage portfolio grew in real terms approximately four times, the increase has not followed a consistent trend during this time interval.

77 See the EMF Quarterly Review Q1 2013 at p. 11.

http://www.hypo.org/DocShareNoFrame/docs/1/JGBMNBBCFIGAGIBODFMIGMHHPDW69DBDGYTE4Q/EMF/Docs/DLS/2013-00042.pdf

The "First House" programme[78] has improved access to mortgage credit, as 53% of the housing loans granted in 2011 and the first half of 2012 were contracted under this program. These loans were almost exclusively (99%) denominated in foreign currency. The 2011 Annual Report of the NBR noted an increase of housing loans (11.8% at the end of 2011 versus 10.6% in December 2010), especially forex-denominated ones, driven by the successive stages of the "First House" Programme.

Starting with the first year of the First House programme, the average amount of the security that a debtor had to give has steadily declined: from €41,574 in 2009, €40,133 in 2010 to €39,115 in 2011 and about €37,500 in the fourth stage of the program. In recent years domestic house lending was supported overwhelmingly by the First House programme. Thus, according to data submitted by the National Credit Guarantee Fund for Small and Medium Enterprises, approximately 74,000 loans, with a total value of €2.9 billion had been granted using the state guarantees until the end of October 2012.

According to statistics of the National Bank of Romania, this amount is very close to the volume of all housing loans contracted during the same period. Thus, if at the beginning of July 2009 the balance of housing loans nationwide amounted to about €5,33 billion, at the end of October 2012 this indicator was approximately €8,25 billion, with €2,92 billion more than before the start of the First House programme.[79]

4. What is the relation between employment and over-indebtedness?

Unemployment[80] is among the most significant macro-economic determinant of over-indebtedness, followed by wages, fluctuations in the interest rate and movements in the exchange rate.[81] Second, the share of the debt service in the monthly gross income of households is relatively high in Romania compared to other EU countries.

a. How many per cent of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when over-indebtedness arose? time when:

i. the credit contract was signed

No data available.

ii. over-indebtedness arose

Proportion of those in households with outstanding debts of over 100% of disposable income by work intensity (% of each group): 0-0.19: 2.9%; 0.20-0.50: 2.2%; 0.51-0.74: 1.1%; 0.75-1.0:1.0%.

Proportion of those in households with income below 60% of the median with outstanding debts of over 100% of disposable income by work intensity (% of each group): 0-0.19: 6.4%; 0.20-0.50: 4.1%; 0.51-0.74:0.2%; 0.75-1.0:1.1%.[82]

b. How has the average salary evolved since 2000?

78 The "First House Programme" is part of the 'anti-crisis' measures initiated by the government to support the priority economic sectors. The main objective is to unlock lending and support the construction sector, which was aimed to have positive effects on the economic activity and create new jobs. Furthermore, the Program was aimed to improve access of the population to mortgages. For this purpose, the state offered to guarantee 50% of the loans granted by banks, provided they give cheaper loans to individual consumers. Legislative framework: OUG no. 60/2009 concerning certain measure on the implementation of the programme "First House" and Decision no. 717/2009 concerning the adoption of the norms implementing the programme "First House".

79 http://www.ziare.com/casa/apartamente/cum-s-au-modificat-preturile-la-apartamente-si-cererea-de-credite-pe-timp-de-criza-1210271

80 On the rate of unemployment in Romanian compared with other EU countries, see Chart 2.3 Unemployment rate in 2013 NBR Financial Report.

81 According to the Financial Stability Report of the NBR of 2013, p. 129 ff.

82 See for more details Research Note 4/2010 Over-indebtedness New evidence from EU-SILC special module, pp.32-43.

In Romania, the real wage[83] and thus buying power increased by 13% in the period between 2000 and 2008, which is the biggest advance registered for that period in the EU, according to a study conducted by the European Trade Union Institute, quoted by EurActiv. On the other hand, between 2009 and 2012 real wages in Romania fell by over 1.7%, placing Romania on the fifth place of EU countries registering the largest decreases in the Union, after Greece, Lithuania, Hungary and Estonia.

5. *Non- EUR countries: Did national monetary policy play a role in consumer credit and mortgage agreements?*

   a. *Are/were foreign currency loans common?*

From 30 June 2000 to 30 June 2001, the largest share, about 65%, of the total mortgage loans, were in RON (situation due, in part, to the impossibility of granting mortgages in foreign currency under Law No. 190/1999). In 2002 with the amendment of Law 190/1999, the household credit market witnessed an increase of mortgage loans in foreign currency, which eventually held by the end of 2002 about 69% of all mortgage loans.

Between December 2004 and December 2007, the highest percentage of household debt consisted of debt service for consumer credit and was in domestic currency. In 2008 the level of debt service in foreign currency came close to the level of debt in domestic currency.

Table no.6

Year	Million RON	Domestic Currency	Foreign Currency
2004	11,874	54.1	45.9
2005	21,371	55.9	44.1
2006	39,271	58.8	41.2
2007	71,508	46.9	53.1
2008	92,210	41.3	58.7

Source: World Bank Diagnostic Review of Consumer Protection and Financial Literacy in levels calculated in percentage in Romania of July 2009

In early 2007, foreign currency mortgages accounted for 85.5% of total mortgage loans to households. Thus, of the approximately 7.9 billion RON lent by banks to customers who wanted to buy a home, the equivalent of six billion was borrowed in euros and 0.7 billion in other foreign currencies, especially Swiss francs and US dollars. At the end of 2007, over half of all household debt was in foreign currency.[84] Seven years later, namely in January 2013, the mortgage loans in foreign currency amounted to the equivalent of 34.9 billion EURs, or 94.9% of the total stock. At the end of the year, in November, the percentage decreased to 92.2% of the total, due to resuming lending in RON, which rose by 68%, from 1.8 billion earlier in 2013, to 3.1 billion in November, according to the latest data provided by the National Bank of Romania (NBR).

According to the NBR Financial Report of 2013: there was a high share of foreign currency debt (68%); real estate and consumer loans secured by mortgages were overwhelmingly granted in foreign currency (95.5% in the case of real estate loans and 91% in the case of consumer loans with mortgages, banks and NBFIs); the flow of new loans by banks was still predominant in foreign currency (56% between January 2011 and August 2012); the population remained significantly exposed to currency risk, which manifested in higher non-performance rates for loans denominated in foreign currencies compared to RON.

83 The real wage is calculated as the ratio between net nominal earnings index and the consumer price.

84 World Bank Diagnostic Review of Consumer Protection and Financial Literacy in Romania, July 2009, p.1.

Consumer loans and loans for other purposes where given mostly in RON, followed at a small distance by loans in euro, and very few in other foreign currencies.

In terms of evolution of household loans in RON and in Euro, the NBR Report of 2012 noted that

"the annual dynamics of the domestic currency component plunged deeper into negative territory during 2012 Q2 and Q3, before improving in the following months on the back of the consolidated growth rate of RON-denominated housing loans, which ended the year at 15.2% versus -7.7% in December 2011. By contrast, the annual dynamics of household forex loans (expressed in EUR) witnessed a quasi-steady decline starting in 2012 Q2, driven by all credit categories, from 4.3% in March to -1.2% in December."[85]

The President of the NACP mentioned that currently (in 2014), a bank has on average 2,000 – 3,000 debtors with credits in Swiss francs or US dollars, the majority of which were contracted in the period between 2007 and 2008.

b. What are the foreign currencies in which loan agreements were concluded?

Loan agreements were mostly concluded in euros, followed by a large percentage difference by US dollars and Swiss Francs. In 2012 more than half of household loans were in euros, loans taken for housing purposes were approximately 90% in euros with the majority of the rest in other foreign currencies, and the remaining smallest percentage in the national currency. In December 2006, the weight of loans in Swiss Francs and Japanese yen was very low (1.4%).

In June 2011, the euro denominated loans accounted to approximately 80% of the outstanding foreign currency loans. Between January 2007 and October 2013, the number of mortgage backed credits contracted in Euros increased every year, while mortgages contracted in RON and other foreign currencies remained in total constant.[86]

However, since 2011, as a result of consumers being more and more aware of the high risks of over-indebtedness associated with credits in euro, there has been an increase in consumer demand for loans in domestic currency. For instance, the share of new euro denominated loans to households shrank considerably in the case of consumer loans (from 35.7% in 2011 to 10.3% from December 2011 to August 2013), and to a lesser extent when looking at housing loans (from 97.8% in 2011 to 86.4% from December 2011 to August 2013).

c. Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?

Yes, due to the increase of the exchange rate of Euro since the start of the financial crisis, taking into account that the majority of loans taken for housing purposes were taken in Euro.

85 NBR Report 2012, p. 39.

86 For more details on the evolution of credit secured with mortgages detailed by currency (total mortgages, mortgages in national currency, in Euro and other foreign currencies) by year between January 2007 until October 2013, see tables provided by the NBR Financial Stability Report of 2008 and 2014.

Table no.7

Year	End of year exchange rates RON-EUR
1996	-0.518
1997	0.886
1998	1.281
1999	1.835
2000	2.414
2001	2.782
2002	3.514
2003	4.116
2004	3.939
2005	3.680
2006	3.384
2007	3.608
2008	4.023
2009	4.236
2010	4.262
2011	4.323

Source: NBR statistical database

The NBR noted in its 2011 Annual Report that:

"Foreign currency loans are a major vulnerability of households. Foreign currency lending increased at a faster pace than loans in domestic currency, thus contributing to a wider mismatch between foreign exchange-denominated assets and liabilities. The credit risk associated with foreign currency loans rose more rapidly than in the case of loans in domestic currency, the dynamics of non-performing loans in foreign currency being faster than that of RON-denominated loans, in the case of households."[87]

The high percentage of household credit in foreign currency is one of the reasons identified by the NBR as a cause for the increasing non-performing loan ratio in 2012. Foreign-currency lending remained riskier than lending in domestic currency for all categories of debtors, as the volume of the non-performing loans in foreign currency increases more swiftly than that in RON. Thus, the high indebtedness level, particularly the one related to foreign currency loans, remains the main vulnerability of households, as their debt-servicing capacity kept declining, albeit at a slower pace in 2012 than 2011. The short foreign exchange position of households towards the banking sector was held by the NBR to be capable of inducing vulnerabilities at the balance sheet level.

The mismatch between foreign exchange-denominated assets and liabilities of households is held to be persistent, although it followed a downtrend in 2012. This trend was registered in spite of the norms enacted by the NBR since 2008, including 2013.[88] The non-performing loan ratio for foreign currency loans stood at 11.1% in June 2013 (versus 8.9% for RON-denominated credit), up 2.5 percentage points from December 2011. The Debt-to-Income (DTI) ratio for consumers with foreign-currency loans was 49%, as compared to 34 % for consumers with home-currency loans in June 2013.

87 2011 NBR Annual Report, p. 29. The NBR noted that "the NBR closely monitors foreign currency lending developments, adopting additional measures for loans in foreign currency to be granted with the adequate management of risks associated with unhedged debtors."

88 See, for example, Regulation nos. 11/2008 and 2/2009 amending Regulation no. 3/2007 on limiting the credit risk for credits granted to individuals, entered into force on August 2008 which required credit institutions to inform consumers on the risks of debt increases due to changes in foreign exchange, interest rates and commissions.

6. Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?

According to NBR Reports, another macro-economic risk that was not mentioned in the above paragraphs was the low confidence in the financing stability.

IX. Micro-economic risk factors for over-indebtedness (consumer behaviour).

1. How many credit agreements do consumers conclude on average?

During the period 2000 – 2002, banks granted mortgages to individuals for the purpose of construction, purchase, rehabilitation, consolidation or expansion of houses, the term did not generally exceed ten years.

Consumers can take loans for non-housing related purposes, such as general consumption, and education, and guarantee with an immovable property. In 2006, the demand for real estate was fuelled to a smaller extent by the mortgage loan. The average value of a mortgage loan was of RON 72,000 (in December 2006), a value that was far below the price of a house. Almost 67% of the mortgage loans had a value that lies below the average house price. Consumer credit per capita: 2005 – 0.197; 2006 – 0.416; 2007 – 0.709; 2008 – 0.851; 2009 – 0.800; 2010 – 0.703; 2011 – 0.670.[89]

2012 started with a decrease in demand for loans for both mortgage and consumer loans, despite banks' previous expectations. In the second quarter the loan demand expanded for both mortgage and consumer loans, in the third quarter, loan demand declined for the mortgage loans, and remained constant for the consumer loans. The year 2012 ended with a decrease of new loans demand from households both for mortgage and consumer loans.[90]

In June 2013 mortgage-backed loans accounted for 60%.[91] While consumer loans accounted for 55.5% of the total loans, 35.5% were housing loans.[92]

2. How many credit agreements do consumers conclude on average?

Table no. 8

Year	Average number of credit agreements concluded by consumers
2008	1.64
2009	1.66
2010	1.63
2011	1.59
2012	1.58
2013[93]	1.58

Source: Credit Bureau, Centre Credit Register

3. Was/is the housing market in the country based on rent or ownership?

89 According to data collected by ECRI Report on Lending to Households in Europe (1995 – 2011) value in EUR.

90 According to the NBR published BLS of May, August, November 2012 and February 2013.

91 According to data made available by the Euromonitor International, http://www. EURmonitor.com/consumer-lending-in-romania/report

92According to the NBR Bank Lending Survey of May and August 2013.

93 In September 2013, there were 1.59 credit agreements concluded per consumer, according to the NBR reply of 14 November 2013 to Project questionnaire. The 1.59 was updated to 1.58 following the reply of the NBR of 26 February 2014.

According to Eurostat statistics, the percentage of private ownership has risen from 5.3 in 2007 to 8.4 in 2013.[94] According to the 2012 Housing Europe Review,[95] in 2012 the housing market was approximately 95% owner-occupied. Desire for home ownership is a strong cultural characteristic in Romania. In the 90s several banks in Romania were actively planning for an expansion of their mortgage lending, including BCR, HVB, Alpha Bank, Raiffeisen and Ro-Fin. In addition, the National Housing Agency (ANL), which acts primarily as a housing development and construction agency, started to provide subsidized loans to eligible borrowers, at first through BCR.[96]

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if data available)?*

In 2006, the loans with a mortgage collateral represented 62% of household loans.[97]

Table no.9

Year	Mortgage agreements concluded per year
2007	52,608
2008	42,665
2009	20,386
2010	34,192
2011	35,898
2012[98]	43,403
January-September 2013	45,698

Source: NBR (reply to questionnaire, 14.11.2013)

Table no.10

Year	Housing loans per capita in thousands of national currency
2005	0.243
2006	0.372
2007	0.659
2008	0.971
2009	1.129
2010	1.350
2011	1.559

Source: ECRI Statistical Package 2013 - Lending to Households in Europe

Table no.11

Year	Housing loans per capita in thousands of

94 Distribution of population by tenure status, type of household and income group (source: SILC)Last update: 05-11-2013 http://appsso. EURstat.ec. EURpa.eu/nui/show.do?dataset=ilc_lvho02&lang=en

95 Housing Europe Review 2012 The nuts and bolts of European social housing systems, published by CECODHAS Housing Europe's Observatory, Brussels (Belgium) October 2011, available at http://www.housing Europe.eu/www.housing Europe.eu/uploads/file_/HER%202012%20EN%20web2_1.pdf

96 The Urban Institute, Developing Secondary Mortgage Markets in Southeast Europe. Assessment of the Mortgage Market in Romania, available at http://www.ceemortgagefinance.org/pdfs/Romania_assessment.pdf

97 NBR Financial Stability Report of 2007.

98 Starting 2012, the data does not include refinanced loans.

	EUR
2005	0.066
2006	0.110
2007	0.183
2008	0.241
2009	0.266
2010	0.317
2011	0.361

Source: ECRI Statistical Package 2013 - Lending to Households in Europe

5. *How many indebted and over-indebted consumers have credit card debt?*

   a. *How high is this debt?/How long does it take consumers on average to repay credit card obligations?*

Table no.12

Year	Number of consumers with credit cards	Debt accumulated by credit card holders (RON)
2008	824,888	1,549,261,859
2009	1,143,581	2,738,466,202
2010	1,154,733	2,781,979,347
2011	1,214,001	2,710,375,165
2012	1,304,042	2,854,450,793
2013	1,300,882	3,232,176,871

Source: NBR (reply to questionnaire, 26.02.2014)

6. *How many per cent of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?*

No reliable data.

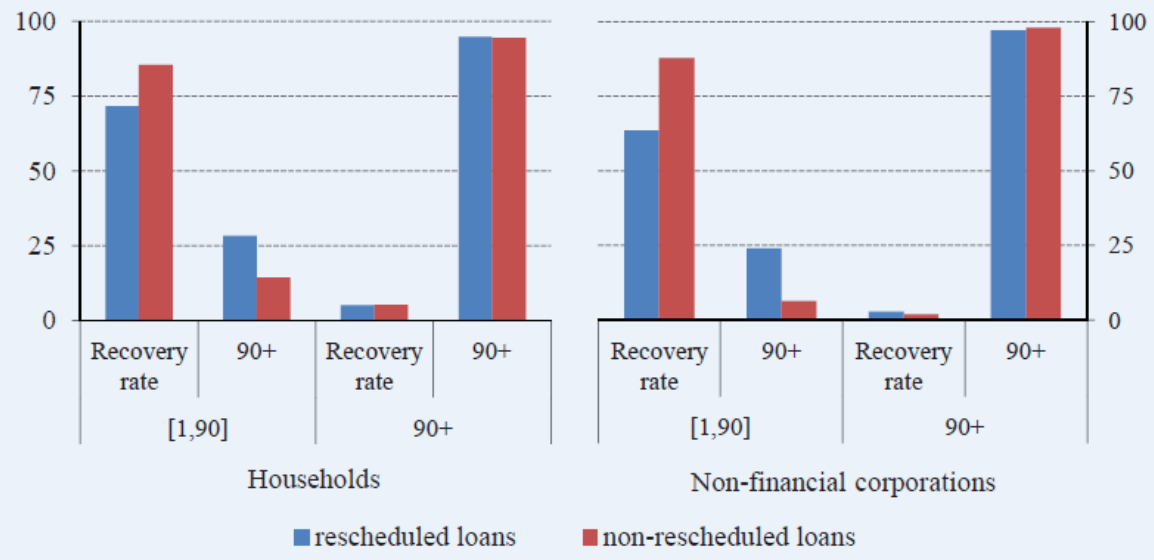
   a. *How high is this debt?*

The volume of non-performing loans (90 days+ delay overdue loans) in June 2013 was of 10.7 billion RON.[99]

7. *How long does it take consumers on average to repay overdraft facility debt?*

99 Data provided by the NBR on 14.11. 2013 in reply to questionnaire.

Average annual probability of transition by overdue bucket for loans worth more than lei 20,000 granted to households and non-financial corporations (June 2013)



Note: For non-performing loans (90+), the recovery rate was assimilated to the exit from this overdue bucket. The analysis looked at the annual evolution of rescheduled loans compared to those for which no contractual changes were made; the initial moment is not necessarily that when rescheduling measures were taken.

Source: CCR, NBR calculations

8. *Is there a relation between the length of the credit obligation and over-indebtedness?*

   a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*

According to the NBR, an inverse proportional relationship was found between the rate of default (non-performing loans, NPL) and the original maturity of the loan.[100]

Table no.14

Year	NPL_tl%[101]	NPL_tm [102]%	NPL_ts %[103]
2008	2.31	4.24	3.80
2009	5.88	9.07	21.79
2010	6.76	13.59	34.77
2011	6.83	14.81	41.59
2012	7.99	15.57	39.48
2013	6.88	22.08	43.42

Source: Credit Bureau, Central Credit Register[104]

100 According to the 2013 NBR Financial Report Chart on Average annual probability of transition by overdue bucket for loans worth more than 20 000 RON granted to households and non-financial corporation data of June 2013: the recovery rate for loans with less than overdue 90 days was 72% of total loans; 80% recovery rate for rescheduled loans with less than 90 days; almost close to 0 recovery rate for both loans and rescheduled loans overdue for +90 days..

101 Non-performing loans out of total loans.

102 Non-performing loans out of total mature.

103 Non-performing loans out of total security.

104 Data provided by the NBR on 26.02.2014, in reply to questionnaire

b. How long are the time periods for which consumers took on credit and mortgage obligations?

According to the NBR Regulation no. 17/2012, mortgage loans cannot be given for a time period of less or equal to five years. According to NBR surveys of 2012 and 2013, the average length of the loan is 22 years for credits secured by mortgages or seven years for consumer credits not secured by mortgages. A similar duration of the agreement, though slightly higher for mortgage credits, exists also for the mortgages concluded between 2007 and 2011.

10.5.1. Outstanding Amounts

(% p.a.)

Period		Loans to households			
		Total	with agreed maturity		
			of up to and including one year	over one year and up to and including five years	over five years
2008		16.59	22.41	17.82	15.22
2009		17.11	20.97	18.61	15.85
2010		14.83	16.48	15.49	14.23
2011		14.00	15.20	14.94	13.42
2012		13.26	14.05	14.16	12.56
2012	Aug.	13.11	13.88	14.10	12.48
	Sep.	13.11	13.85	14.10	12.45
	Oct.	13.23	14.07	14.16	12.56
	Nov.	13.23	13.97	14.18	12.54
	Dec.	13.26	14.05	14.16	12.56
2013	Jan.	13.35	14.26	14.15	12.66
	Feb.	13.34	14.22	14.18	12.7
	Mar.	13.37	14.35	14.34	12.56
	Apr.	13.05	13.91	14.01	12.27
	May	12.91	13.79	13.84	12.11
	Jun.	12.76	13.71	13.66	11.93
	Jul.	12.47	12.90	13.64	11.57
	Aug.	12.46	12.72	13.71	11.50

c. What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?

No data available.

X. Relation between income and (over-)indebtedness

1. How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?

The share of consumer spending for meeting basic needs, more exactly for purchasing food items, is significantly higher for Romanian households than the EU average (44.2% compared to 16.8% in 2005, with a decrease to 35% in March 2013). The occurrence of unfavourable developments in the interest rate or the exchange rate can be more difficult to manage when there are constraints on disposable income and savings increase only gradually.

Table no.15

Table no. 3 Total expenditure and consumption expenditure pattern of households

Year	2001	2002	2003	2004	2005	2006	2007	2008
Total expenditure	516,52	651,66	781,45	1049,94	1149,33	1304,66	1541,96	-
The share of total expenditure in total income (%)	98.99	98.95	98.28	96.69	94.81	94.11	91.42	-
Index of total expenditure % (100 = previous year)	100	126,16	119,91	134,36	109,47	113,51	118,19	-
Total consumption expenditure lei/month/ household	376,51	474,47	566,87	752,00	863,89	962,50	1104,70	1365,36
Consumption expenditures index % (100 = previous year)	100	126.00	119.47	132.66	114.87	111.41	114.77	123.59
Share of consumer expenditure in total expenditure (%)	72,89	72,81	72,54	71,62	75,16	73,77	71,64	-
The structure of consumption expenditure								
Food products and soft drinks	52,2	49,9	48,6	46,4	44,2	42,3	41,7	40,9
Alcoholic beverages, tobacco	6,0	5,9	6,3	5,9	5,8	6,0	6,5	6,5
Clothing and Footwear	5,9	6,1	6,1	6,3	6,2	6,2	6,8	6,7
Housing and endowment of goods	16.4	17.8	18.3	18.5	19.4	20.4	20.1	20.4
Health	2,7	2,8	3,0	3,6	3,8	4,1	3,9	4,1
Transport and communications	9.2	9.6	9.4	10.6	11.4	11.6	11.0	11.1
Recreation, culture, education	4.4	4.5	4.6	4.8	5.1	5.2	5.4	5.3
Other expenditure	3.2	3.4	3.7	3.9	4.1	4.2	4.6	5.0

*Source: calculations based on data from ***, Romanian Statistical Yearbook 2008; ***, Romania in cifre 2009; www.insse.ro*

The main destination of household expenditure was consumption, which was more than 70% of total expenditure of households. The share of expenditure for food consumption in Romania was high, over 40%. This can be explained by the low standard of living of the majority of the population, but due to increasing real incomes of the population, it registered a downward trend in the period under review.[105]

The figures for the total credit to households as a percentage of final consumption expenditure of households are: 1996 -10.07; 1997 - 0.83; 1998 –1.03; 1999- 0.65; 2000 - 0.63; 2001- 0.98; 2002 - 2.01; 2003- 5.74; 2004-6.95; 2005 – 10.64; 2006 - 16.64; 2007 – 25.69; 2008 -29.72; 2009 - 32.50; 2010 – 31.40; 2011 - 28.49.[106]

The figures for the total credit to households as a percentage of disposable income of households are: 1996 –-9.57; 1997 - 0.83; 1998 –1.13; 1999 - 0.69; 2000 - 0.63; 2001 - 0.96; 2002 – 2.63; 2003 - 6.29; 2004 - 7.41; 2005 -11.92; 2006 - 18.85; 2007 - 28.65; 2008 - 30.05; 2009- 32.17; 2010 - 33.57.[107]

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*

105 Income and expenditure of households in Romania, by Prof. Laura Cismaș Ph.D., assistant Andra Miculescu Ph.D., assistant Maria Oțil Ph.D. (West University of Timisoara, The Faculty of Economic and Business Administration, Romania), paper available online at http://feaa.ucv.ro/AUCSSE/0038v1-002.pdf

106 Source: ECRI Lending to Households 2012 Report.

107 *Ibid.*

There are two current parallel trends in the credit service market. First, the amount of instalments in the case of low-income debtors with mortgage agreements is very often higher, due to the fact that they are the category of consumers experiencing the highest level of over-indebtedness. Moreover, there is a list of additional costs that low-income debtors will need to pay, regardless of the re-organisation or re-financing measure they benefit from (see section VI). Another, more recent trend, is that banks have found as a strategy for compensating their financial losses resulting from maintaining low costs of administration of loans for over-indebted low income debtors, by increasing the costs for the administration of loans for those debtors who are good payment clients.

a. *Do lenders consider low-income to be more likely to default and attempt to mitigate this risk through higher interest rates?*

A positive reply can be inferred from practice.

b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*

Taking into account that the highest percentage of over-indebted consumers are those with low income, if the bank decides to transfer the non-performing credit to a private company which applies high interest and fees for re-evaluation of the credit, then it may well happen that this category of low income debtors will end up paying more and/or higher interests for mortgage agreements than the high income consumers. For mortgage secured credits contracted between 2007 and the beginning of 2011, some banks used to insert also a default risk clause in the contract, which has subsequently been subject to court litigation, due to the possibility to unilaterally change the percentage provided as a default risk and also the unclear method of calculation of the risk default (see more in the Litigation section).

c. *Are there other key terms which change according to the income of the borrower?*

Behaviour of actors in relevant cases

XI. Irresponsible lending practices

1. *Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)*

In practice the initiator of the relationship is both the creditor, through advertising channels, and also the consumer. The relationship between the lender and borrower was influenced by public policies that promoted the purchase of a house (the 'First House programme' described at VIII.3 above), and thus encouraged the debtor to approach lending institutions. At the same time, lending institutions advertised their promotional offers for loans.

2. *Was a creditworthiness assessment undertaken before granting the credit?*

a. *In how many cases were creditworthiness assessments undertaken?*

The National Authority for Consumer Protection (NACP) pointed out that before the start of the crisis in Romania, a very high number of credits were given based only on the presentation of the national identity card.

Without giving numbers, the NACP acknowledges in its answer to our question a difference after the start of the financial crisis and entry into force of the Government Emergency Ordinance no. 50/2010

(OUG 50/2010) on credit agreements for consumers (which transposed Directive 2008/48/EC), due to the legal provision therein (see below)[108].

b. Who was the initiator of the creditworthiness assessment?

According to Article 30 of OUG 50/2010, the creditor should be the initiator. In practice, in the years of the economic boom (2007, 2008), the lending institution did not thoroughly assess creditworthiness. With the financial crisis, the consumer started to be more aware of the importance of a creditworthiness test, especially in cases of long-term credit for housing purposes. With the raise of over-indebtedness starting with 2009, both banks and consumer were initiators.

c. Who undertook the creditworthiness assessment?

The creditor – lending institution, in collaboration with the Credit Bureau, which provides data on the indebtedness situation of the consumer (see VII above).

d. What were the criteria of the creditworthiness assessment?

The lending institution usually takes into account more factors to assess the financial situation of the debtor: the duration of the loan (mortgage), for the purpose of calculating the age of the debtor at the end of the contract (if the loan period needs to continue after the debtor reaches 65 years old, the credit demand is usually refused); the duration of the employment contract of the debtor; the position of the debtor at work; the monthly salary of the creditor; the debtor's age and health; the type of guarantees the debtor can bring for the loan (whether the debtor can pledge in another good than the apartment (s)he intends to purchase with the loan); the status of the block of flats where the apartment to be mortgaged is located, and the date when it was put into use.

e. Was a credit bureau involved?

No data available.

3. Is there a legal obligation for a mandatory creditworthiness assessment? Is this obligation observed in practice?

Creditworthiness assessment is obligatory when needed to obtain sufficient information on the creditworthiness of the consumer, according to Article 30 of the OUG 50/2010. Furthermore, Article 31 provides the involvement of credit bureaus in cases of cross-border transfer of credit:

> "in view of assessing the creditworthiness of consumers, evidence type of systems such as credit bureaus ensure, in cases of cross border credits, access for creditors from other Member States to databases in conditions equal to those provided for national creditors."

The involvement of credit bureaus is also mentioned in Article 32:

> "(1) If the credit application is rejected based on consultation of a database, the creditor shall inform the consumer immediately and free of charge, in writing or at the express request of the consumer, in the format chosen by him and approved by the creditor, about the outcome of this consultation and the identity of the database consulted. (2) This information shall be provided, unless the provision of such information is prohibited by national standards transposing European legislation or create the legal framework for its application or provide information contrary to objectives of public policy or public security."

4. Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?

Creditworthiness rules were less strict before the start of the crisis. While in the period before 2001 there were no specialised creditworthiness rules for households.

108 Reply of the NBR to questionnaire, of 26.02.2014.

In the unfavourable economic context, and following the new wave of regulations adopted by the NBR in 2011 and 2012, banks have adopted a cautious stance on granting new loans, preferring operations restructuring or refinancing loans.[109]

Chances of contracting a new loan are reduced if the consumer has outstanding payments in the credit bureau database. If a natural person exceeds the limit of 30 days for the payment of the instalment, they are registered by the Bank to the Credit Bureau (CB) and /or the Central Credit Register (CCR) as a "bad debtor". Most banks used to lend to people with delays of up to 60 days and with smaller amounts of 100 RON, according to the rules of each bank.[110]

However, the decision belongs to each individual bank. In fact the registration of a person in the Credit Bureau database does not automatically deprive the consumer of the possibility to contract a new loan.

There is no specific data on the number of refusals based on the negative outcome of the creditworthiness assessment.

5. Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?

A survey from December 2006 showed the following aspects are among the main complaints of bank credit consumers in Romania: the absence of sufficient information prior to the signing of a loan contract; bank staff being unwilling or unable to assist consumers who did not understand bank terminology, and terminology being too specialized an difficult for a consumer to understand.[111] Further, these complaints persisted in 2008 and 2009 when they were addressed by the NBR via specific Regulation (Regulation 11/2008, and 2/2009).

6. Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?

Consumers felt pressured in the sense they could not negotiate the contractual conditions of their loan, since these conditions are imposed by the lending bank.[112]

XII. Irresponsible borrowing practices

1. Did the consumer read the agreement before signing?

In spite of the numerous specific legal provisions including several guarantees aimed at ensuring that the consumer of bank credits reads and understands his rights and obligations before signing it,[113] there

109 Source: http://www.efin.ro/, a website that provides financial information.

110 Reply of the NBR to questionnaire, of 26.02.2014.

111 S. Cani, Establishing a Bank Ombudsman in Romania: Background Study prepared for the SPI Committee. Convergence Programme.

112 This is the common reply given to this question by interviewed consumers.

113 See Art. 11(2)(a) of OUG 50/2010GEO which imposes a binding period of fifteen days before the consumer concludes the credit contract, in which period they are given all the relevant information on the future contract. The information to be written into the credit agreement have to follow a certain style, format, and fulfil certain objectives so that the consumer can form a learned opinion of the obligations to reimburse the credit, as provided by Article 33 Paragraph 1 of the GEO no. 50/2010.Article 33(2) of the GEO provides:…(2) Credit agreements shall contain comprehensive, clear and easy to understand, in Romanian. This information will be further detailed or explained by the bank, at the express request of the consumer, before signing the contract in the form of notes, annex to the contract.' According to Article 34 of GEO no. 50/2010, at the moment when the contract is concluded all contracting parties receive one original of the credit agreement, except for the distance contracts. NBR 17/2012 Articles 6-11 provide that the creditor is obliged to inform potential borrowers of the severe impact of a possible depreciation of the national currency on the level of regular payment of their obligations "for loans in foreign currency " Moreover, "lenders and institutions referred to in Article 1

are numerous cases in practice where the consumers have complained of not having been explained the precise conditions of the contract before signing it; or that the provisions of the contract were so technical and lacunar that they could not be understood by the average consumer.

2. *Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?*

Before taking a loan, consumers normally compare the offers of several banking institutions either on online financial specialised web search engines,[114] or in person at the banks.

3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*

The consumers were commonly offered the possibility of asking more detailed information before signing the credit contracts, and information was given. However the level of financial education is low, and some of the loan risks of the credit become evident only one or two years after the conclusion of the agreement and after the financial crisis, such as the depreciation of the national currency in relation to the foreign currency on which the credit was denominated.

4. *How much time did the consumer take before signing the agreement?*

No data available.

5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

Consumers make use of the right to withdrawal very rarely.[115] Article 58 of OUG 50/2010 gives the right to the consumer to withdraw in fourteen days from one of the following dates: a) the conclusion of the credit; b) the date on which the consumer is made aware of the terms and conditions of the contract at a time later than the date at letter a).

Litigation

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*

Yes. There has been litigation before courts of all levels, including the High Court.[116] So far eight preliminary references[117] on the interpretation of provisions of Directive 93/13/and Directive 2008/48 were sent to the CJEU in proceedings concerning loan agreements.

(Contd.)

Paragraph (2) provide the information referred to in Article 7 on paper or another durable medium, at least 15 days before the conclusion of the credit agreement."

114 An example of such a search engine is http://www.conso.ro/compara/credite-imobiliare

115 Based on interviews with consumers.

116 According to procedural rules establishing competence, in private proceedings (not involving the NACP) the amount in dispute is one of the criteria determining which court is competent to hear a case. Thus both local courts and county courts may hear cases in first instance. Therefore, if a case started before the county court, the second appeal will be heard by the High Court of Cassation and Justice (the supreme court of Romania).

117 At the time of writing, out of a total of 62 since Romania's accession to the EU, 8 regarded consumer protection in credit agreements secured by mortgages concluded with banks: C-92/14; C-143/13, Matei and Matei; C-236/12, SC Volksbank România; C-123/12; C-108/12; C – 571/11; C- 47/11; C-602/10.

Additionally, the Constitutional Court rejected on the merits the pleas of unconstitutionality of the national law transposing Directive 2008/48, that were raised in several proceedings concerning loan agreements granted by banks to individual consumers.

a. What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?

The main legal norms invoked in litigation were[118] Law 193/2000 on the protection of consumers regarding unfair terms in contracts and Government Emergency Ordinance 50/2010 (OUG 50/2010) on credit agreements for consumers.

As described above at IV.1, Law 193/2000 is a national statute adopted for the purpose of ensuring the protection of consumers against unfair terms in contracts and transposes Directive 93/13. It has the nature of a special law compared to the provisions of the Civil Code on contracts and therefore its provisions take precedence over the latter.[119]

OUG 50/2010 was adopted for the transposition of Directive 2008/48 into national law and was amended soon after its entry into force.

Courts are by now well aware of the fact that both acts contain provisions that reflect provisions of EU origin and therefore are very careful to interpret and apply them in a manner consistent to their parent Directives as interpreted by the CJEU. If awareness among the judiciary about pre-accession case law interpreting Directive 93/13 such as Joined Cases C-240/98 to C-244/98, *Océano Grupo Editorial* was raised slowly, by the time of the adoption of OUG 50/2010, the publicity surrounding it and its nature as an act reflecting an EU Directive greatly contributed to making its compatibility with the Directive a forefront issue from the very beginning.[120] This prompted the referral of a series of repetitive questions from all different regions the country concerning the extension of the material and temporal scope of Directive 2008/48 by OUG 50/2010. The CJEU answered these issues in case C-602/10, *Volksbank*.

Law 193/2000 provided the main cause of action for private plaintiffs before the adoption of OUG 50/2010. Afterwards, the OUG became the focus of litigation involving the practices of mainly one bank. They are sometimes used together, depending on the type of plaintiff and proceedings (see below).

b. What were the issues in question? (i.e.: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)

The main issues in question, each of them typical to contracts concluded by a particular credit institution, are:

- The potential unfair character of the unilateral increase of the variable interest rate by the credit institution.
- The issue whether a particular commission may be characterised as part of the "price" of the financial services provided so that its adequacy may not be subjected to judicial control under Article 4(6) of Law 193/2000 which literally transposes Article 4(2) of Directive 93/13.
- The legal effects of a finding of unfairness of a contractual term.

118 Consumer's claims alleging unfair credit agreements against banks are still pending before national courts, however these credit contracts usually date from the same period 2006-2009.

119 The authority in charge with the task of ensuring the observance of Law 193/2000 is the NACP (Art. 8 Law 193/2000).

120 See D. Efrim, M. Moraru and G. Zanfir, The Hesitating Steps of the Romanian Courts Towards Judicial Dialogue on EU Law Matters, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2261915

- The legality of a particular type of commission.[121]
- The nature of the obligations of the assignee in the event of assignment to a third party of the creditor's rights under a credit agreement or the agreement itself.

2. *Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?*

In some cases, individual plaintiffs brought cases asking for the annulment of the unfair terms from their credit contracts against the lending institutions directly before the courts.

In other cases, individual plaintiffs first made use of the administrative complaint procedure prescribed by Law 93/2000 on unfair terms in consumer contracts before the National Authority for Consumers' Protection (NAPC). Upon application of sanctions by the NAPC, the financial institution challenged the administrative act before the courts. There is also a line of cases where the issue of unfair terms in credit contracts was raised directly during enforcement proceedings initiated by creditors or assignees against the individuals.

3. *What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?*

No official data is available that covers the entire country.[122] Since 2010, there have been thousands of cases related to mortgage agreements between consumers and banks raised before the National Authority of Consumer Protection and/or national courts.

The total amount of the fines determined by the NACP in 2008 against credit institutions was of approximately €210,000.

In 2010 the NACP had approximately 140 complaints of unfair clauses lodged against the majority of national banks. The fourteen complaints finalised until August 2010, were won by the NACP on behalf of the consumers.[123] Fines in the amount of 380,000 RON (€90,000) were applied by the NACP. The director of the NACP stated that 70% of the registered claims were approved.[124]

According to the President of the NACP, between 2008-2013, the NACP finalised around 750 cases before courts against different financial institutions on the basis of Law 193/2000, of which the NACP won 571 cases.[125] While centralised hard data is not available, it can be stated that the number of cases brought by individuals before the courts are in the thousands (one bank alone was involved in over 2,000 cases).

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121 OUG no. 50/2010 provided an exhaustive list of commissions which banks could charge in relation to consumer credits: e.g. the analysis fee, the credit management, the account management for early repayment, the security costs, penalties, single fee for services provided to the consumer's demand. This legal text left no room for interpretation in terms of the precise list of legal commissions in consumer credits.

122 There is no comprehensive database of case-law in Romania, but only local databases serving each court (approximately 100 which would have on their docket relevant case-law), which are not interconnected and which can be checked only on local computers. Relevant case-law is not archived under a particular heading and therefore data cannot be extracted by way of a keyword search.

123 The President of the NACP declared that "We have not lost any case, because each time we found the right formula. We very carefully analysed the cases and acted only where banks did not operate correctly. The high number of complaints on unfair terms and lack of transparency were the reasons for which the provisions of the European directive [Directive 2008/48] were extended in Romania." Declaration available in Romanian on http://acbdr.wordpress.com/

124 According to an article on the website of the Association of Bank Clients in Romania, http://acbdr.wordpress.com/tag/restante-credite/

125 http://www.gandul.info/financiar/anpc-are-procese-pe-clauze-cu-toate-bancile-mai-putin-una-si-le-va-transforma-in-actiuni-colective-11447829.

Eight out of total sixty-two preliminary references sent by Romanian courts (up to the time of writing) were registered at the CJEU under the 'consumer protection legislation' category. The origin of these preliminary references were cases brought before national courts by lending institutions challenging the sanctions applied by the NACP in consumer or housing credits secured with mortgages or cases brought by individuals for the annulment of unfair terms against the credit institutions.

4. *Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests?*

There are two types of proceedings, laid down by Articles 8-13 of Law 193/2000 on the protection of consumers regarding unfair terms in contracts, initiated by either the National Authority for Consumer Protection (NACP) or consumer associations.

First, NACP[126] has the competence to initiate investigations into the practice of financial institutions and, upon a finding that the contracts under inspection include unfair terms, it must file an action before the competent court asking it to order the removal of the unfair terms from the contracts in progress. Second, with the entry into force of the new Code of civil procedure, the revised version of Law no. 193/2000 conferred, since October 2013, consumer associations the right to file a claim against sellers of goods or suppliers of services who use unfair terms in their consumer contracts. Before this type of action was introduced in Romanian law, there was an instance where consumers who concluded contracts with the same bank organised themselves and used the procedural means provided by the Code of Civil Procedure to achieve as close a result as possible. To this end, they filed actions individually and subsequently asked the court to join them based on similarity of object. However, this led to protracted proceedings and limited legal effects. The judgment applied only to the specific contracts under discussion.

In both types of proceedings, if the court deems that the contract comprises unfair terms which are damaging to the consumers, it can order the supplier (i) to modify all of its on-going contracts containing unfair terms by removing such unfair terms from the contract, and (ii) to remove the unfair terms from all its standard contracts. Furthermore, the court will also order a fine of no more than RON 1,000 (approximately €227) to the supplier that used unfair provisions in its contracts with consumers.

A judicial decision rendered as a result of a collective claim, which orders the removal of unfair terms from all the standard contracts of a certain supplier, will have only limited effects, as it will be limited to the contractual relationships between that particular supplier and its consumers. This means that other professionals who use the exact same unfair terms in their standard contracts will not be affected by a judicial decision delivered against them directly. In theory they could continue to use such unfair terms in their contracts.

If yes:

a. *How are those interests defined?*

There is no specific definition of these interests. Article 37 of the Code of Civil Procedure only provides that, in cases expressly laid down by the law, organisations, institutions and authorities that cannot otherwise justify personal interest may file actions or otherwise participate in proceedings with a view to protect "a group interest" or "a general interest". Articles 8-13 of Law 193/2000 mentioned above would represent such an instance where a special law gives standing to others than the specific injured individual.

b. *What are the requirements for such representation?*

126 NAPC is the public institution with legal personality, functioning under the direction of the Ministry for Economy, Commerce and Environment, which is responsible for the coordination and implementation of governmental policy on the protection of consumers.

The consumer has to first file a claim arguing the unfair term of a contract before an association for the consumers' protection.[127] If convinced, the association will then proceed with the sanction/court representation. (Article 12(3) Law 193/2000)

5. In practice, is litigation in "public / diffuse interest" more common than individual litigation?

No.

6. Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?

Yes. Article 85(2) of OUG 50/2010 transposing Directive 2008/48 refers the consumer to the general out-of-court settlement procedures provided by Law 192/2006 on mediation. Article 85 does not make recourse to mediation as a pre-condition for court actions. Consumers may choose to file an action in court directly. Consumers of bank credits can submit complaints before three bodies.

- The National Authority for Consumer Protection is the main institution that can help private clients dealing with banks. There is also a special provision for situations which fall only under the scope of application of OUG 50/2010 on credit agreements for consumers, and not that of Law 193/2000 on unfair terms. In these circumstances, NACP has the power to find that the financial institution is in breach of OUG 50/2010 and can apply administrative sanctions, which may be appealed before the competent court.
- The National Authority for the Supervision of Personal Data Processing is a public institution with powers limited to situations where a client is abusively registered in the database of the Credit Bureau. The Supervisory Authority may conduct investigations ex officio or upon complaint, and impose fines for misreporting including against the Credit Bureau.[128] In 2009, the National Authority for the Supervision of Personal Data Processing applied fines to four local credit institutions for the first time. The Authority may order the deletion of a client from the database of the Credit Bureau, when it finds that the customer registration was improperly made. A similar sanction was applied by the National Consumer Protection Authority, in 2009, excluding dozens of bank customers from the Credit Bureau database.
- The Association for Consumer Protection, which is an NGO, can also act as arbitrator between customers and service providers, including local banks. "Basically, there are two ways we can help bank's customers in conflicts they have with credit institutions. The main route is arbitration - mediating conflicts between the bank and customer. A second way would be the trial, but in this case we proceed only if it is a group of customers, for example 20-30 people have the same problem. Otherwise the financial effort is not justified."[129]

A fourth settlement body was envisaged to be established in 2007 and 2008 by the representatives of the Romanian Banks Association, which was supposed to have the task of mediation between banks and their customers. It was envisaged in the form of an ombudsman body, similarly to the one existing in countries like the UK, and also present in the department of one of the largest bank in Romania, BCR, although, in a smaller size. So far, this separate arbitration unit has not been established.

7. Do consumers make use of out-of-court settlement procedures?

If yes:

a. Which ones?

127 Arts. 30 and 31 of OUG no. 21/1992 republished defines is an association for the protection of consumers.

128 Statement of Alina Săvoiu, head of the legal department of the National Authority for the Supervision of Personal Data Processing, available in Romanian at http://acbdr.wordpress.com/

129 According to a declaration of the Association for Consumer Protection in Romania representatives from early 2010.

All of the aforementioned three institutions, with predilection for the NACP, also due to the wide mediatisation of its high success rate in its proceedings against lending institutions.

b. What is their success rate? \What are the issues?

In 2009, the Association for Consumers' Protection has dealt with 328 cases in the field of financial services, solving 305, i.e. 93% of all the lodged cases were amicably settled. Similarly with the complaints received by the NAPC, the most frequent complained situations related to increasing interest rates, charging of additional fees that had not been foreseen in the original contract or the presence of unfair contract terms designed to enable financial institutions to unilaterally modify the costs of the loan. Basically, this latter situation refers to the famous clauses whereby banks provided to "reserve the right to change the interest rate based on the market conditions."

Other complaints related to problems concerning the extended period of times in handling complaints by the banks, inflexibility in relation to customers, which have injured the customers.

8. Are there special bankruptcy courts? What is their role?

There is no law on personal bankruptcy.

XIV. Impact of the crisis on litigation

1. Has there been an increase in litigation since the financial crisis?

a. How many mortgage agreements where challenged in out-of-court or judicial proceedings before and after the crisis?

The financial crisis has influenced the depreciation of the national currency in relation to foreign currency, coupled with the high number of credit agreements contracted in foreign currency, and the activation of the risk commission by lending institutions, it thus led to an increase in consumer complaints before judicial and non-judicial bodies. Other important criteria which directly contributed to the raise of litigation, was the entry into force of the OUG 50/2010 which initially applied to all pending credit contracts, even if concluded before its entry into force, and awareness raising of consumers' rights in relation to lending institutions.

The number of complaints from consumers of bank credit agreements increased in the 2000s, reaching a peak of 4000 complaints registered in 2008 at the National Authority of Consumer Protection (NACP). Of this amount, half of the complaints were registered in October of that year, when banks started to unilaterally increase the interest rates in their credit agreements secured with mortgages.

Within the first 6 months of 2009, the NACP received 1250 complaints from consumers of bank credit agreements. Most of these complaints reported an increase of the rate of interest (see answer below), even if the market indicators were decreasing, or refusal to give loans without providing justification. The number of complaints of consumers against banks alleging unfair terms continued to be high until 2012, and since then it is slowly decreasing. The cause of this decrease is, most probably, the fact that these complaints have as object a similar type of credit agreement concluded in the period of financial boom (2007-2008).

b. What are the issues challenged? In which legal field?

Before the NACP, the most common type of complaint relates to the illegal increase of interest rates and commission, the introduction of commission that was not initially included in the credit agreement, closure of accounts that are not timely operated, and misleading promotions such as bonuses on deposits or low initial interest. And as mentioned above, a considerable part of these complaints were finalized by the NACP with application of fines to credit institutions.
Before the courts, the following issues were challenged:

- The potential unfair character of the unilateral increase of the variable interest rate by the credit institution.[130] This type of litigation has been initiated by plaintiffs but has also made the object of investigation and sanctioning by the National Authority for Consumer Protection (NACP). Currently it is winding down as the issue was resolved in favour of the consumer.
- The issue whether a particular commission may be characterised as part of the "price" of the financial services provided so that its adequacy may not be subjected to judicial control under Article 4(6) of Law 193/2000 which literally transposes Article 4(2) of Directive 93/13. Some of the courts dealt with this issue as a matter of national law, analysing the nature of this commission as part of the total cost of the credit, and the outcome was divergent on the substance of the matter. Other courts sought the concrete interpretation of the CJEU and referred very specific questions on this matter.
- The legal effects of a finding of unfairness of a contractual term. For quite some years the jurisprudence of the national courts was divided on this matter. Some of the courts developed a jurisprudence whereby they modified the contract by revising the content of the unfair term, instead of setting it aside (a point of law similar to one of the points discussed in C-618/10, *Banco Español de Crédito*).
- The issue whether the extension of the material and temporal scope of Directive 2008/48 by its transposition law was within the margin of discretion of the State. As explained above, the transposition law included in its material scope credits secured by mortgages and, initially, applied to contracts in progress. It also listed exhaustively the types of commissions a bank may charge. All these issues, which were challenged by banks in courts (particularly one bank), were dealt with by the CJEU in C-602/10 *Volksbank* (I).[131] The Court interpreted the relevant provisions of the directive in the sense that its maximum harmonisation nature applied only to the contracts within its scope, therefore in the absence of other EU legislation, the State was free to regulate other matters not covered by the directive, such as the type of commission a bank may charge.[132] The Court's ruling would have probably led to an outcome favourable to the consumer, the referring court dismissed the case.[133] The reason for the dismissal was the referring court's interpretation of the change in national legislation which occurred shortly after the date the preliminary reference was sent to the CJEU and before the delivery of the preliminary ruling. According to Law 288/2010 approving with amendments OUG 50/2010, the obligations imposed on lending institutions under the Ordinance would no longer apply to contracts in progress, except in very limited exceptional situations, but only to future credit contracts.[134] Thus the national court applied the constitutional principle of the more favourable law applicable to administrative and criminal

130 Lending institutions had 90 days from the entry into force of the OUG 50/2010 to amend this clause.

131 Judgment of 12 July 2012, not reported yet. In this case, a Romanian bank, Volksbank Romania, included in the loan contract a 'risk charge' equal to 0.2% of the balance of the loan which had to be paid monthly by the consumer throughout loan term. This type of charge was provided by this bank as a standard clause in its loan contracts. The regional Romanian consumer protection authority considered this charge as contrary to the OUG 50/2010 (transposition law of Directive 2008/48) and imposed fines on Volksbank for using it. Cases like this one that reached the CJEU were thousands. According to the Romanian law which transposed the Directive, the creditor is only allowed to levy certain, specified in the law charges on consumers and a 'risk charge' is not one of them. Volksbank claimed in front of national courts that the national transposition measures are contrary to the Directive and that at the moment when the credit was concluded, namely before the entry into force of OUG 50/2010, the risk charge was legitimate.

132 Except for the newly entered preliminary reference of 2014, most of the references were either withdrawn by the referring courts as parties reached settlements, or addressed similar issues as those in C-602/10.

133 Judgment of the First instance court of Calarasi of 26.11.2012.

134 This Law was unsuccessfully challenged as unconstitutional, Decision of the Romanian Constitutional Court no. 1656/2010, published in the Official Journal of Romania, 31.01.2011.

offences and annulled the NAPC's administrative act imposing sanctions to the bank, without further discussion on the merits.[135]

2. *Did the Aziz ruling have an impact on national legislation / legal framework?*

   a. *Are there cases before national courts dealing with issues that also arose in the Aziz case?*

As we cannot provide official data on whether parties actually try to bring into their arguments the judgment in *Aziz*, these considerations remain theoretical for now.

Romanian law (Article 718(1) of the CCP) gives the court the power to stay the enforcement proceedings for 'reasonable grounds'. The discretion conferred to the judge may lead to a stay of proceedings in a situation where the debtor introduces a plea that the contract includes an unfair term that had not been brought before. However, while the court enjoys discretion regarding the evaluation of the grounds for ordering a stay of enforcement proceedings, the mandatory condition laid down in Paragraph (2) of the same article may raise problems. The person that asks for a stay of proceedings must lodge a deposit in an amount that varies according to the value of that which is in dispute within the objection to enforcement proceedings. The payment of a deposit as a precondition for a stay of proceedings may represent an obstacle for the debtor who is over-indebted. There is currently divergent jurisprudence on the payment of the deposit in cases where the debtor is in difficulty, but not by reference to *Aziz*.[136]

The possibility under Paragraph (4) of the same article to order immediately a stay of proceedings as a matter of urgency, while the request to stay the proceedings is better evaluated, depends on the same condition of lodging a deposit.

   b. *What was / is considered an unfair contract term in the national court rulings before and after Aziz?*

See point a. above.

   c. *Did Aziz have any other impact on national legislation / legal framework (i.e. in the field of procedural law)? What are those impacts?*

Not yet, according to the collected data.

3. *Is there another case of the CJEU adjudicated after the financial crisis that had a pivotal impact on the national legal framework? Elaborate.*

Not yet, according to the collected data.

Policy / Judicial responses

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

135 Many other similar judgments were delivered by courts from different regions of the country, based on the principle of application with priority of the more favourable law laid down by Article 15(2) of the Romanian Constitution. See, for example, judgment of the Tribunal of Valcea, of 8.09.2011. However it seems they do not entirely follow the judgment of the Constitutional Court in regard to the application in time of Law 288/2010, which concluded in a plea of unconstitutionality raised by a branch of the NACP, that the said Law applies only from its moment of publication in the Official Journal.

136 10% for a value under 10,000 RON; 1,000 RON plus 5% for anything over 10,000 RON; 5,500 RON plus 1% for anything over 100,000 RON; 14,500 RON plus 0.1% for anything over 1,000,000 RON.

Changes in the legal enforcement procedure under the new Code of civil procedure entered into force in February 2013. They concern consumer protection without necessarily enhancing it. In light of the changes introduced by the Code of Civil Procedure on the legal enforcement procedure, shortening the length of the procedure, and in light of the high non-performance rate of bank credits, several banks, including the leader of the bank sector have contracted more external firms to handle the credit recovering.

Some of the most important changes to the procedure of legal enforcement which have considerably shortened the procedure starting with the entry into force of the new Code of Civil Procedure are: 1) shorter period for the enforcement officer to submit the request to admit the start of the legal enforcement procedure before a court (only 3 days); 2) the seized court has to decide on this request in maximum of 7 days; 3) the motivation of the judgment to admit or reject the request to approve the start of the legal enforcement procedure is also limited to a maximum period of 7 days. None of these periods was provided before 2013, and the practice was divided, depending on the number of cases a court would have. Furthermore, some of the previous steps in the legal enforcement procedure have been eliminated, for example, there is no need for the special procedure that confers enforceability to it ("*investirea cu formula executorie*"); also there is only one level of appeal and not two as before, and the time period of appeal has also shortened to 5 days.

In these conditions, unlike before, the banks found it more advantageous to have recourse sooner to the legal enforcement procedure then to insist on the restructuring and re-evaluation procedure.

Since October 2013, collective action by consumer protection association is possible under the revised Law 193/2000 (see section XIII.4 above).

The National Bank of Romania (NBR) adopted several norms increasing consumer protection in relation to lending banking and non-banking institutions. Starting with August 2008, the National Bank of Romania has implemented new prudential requirements aimed at ensuring *ex-ante* that borrowers could deal with unfavourable interest rate and exchange rate developments and, as of 2011, the requirements have extended to also cover the risk of a decrease in disposable income.

The NBR has also revised the regulation applying to lenders, which focuses on attempting to ensure that over-indebtedness does not occur. For example, the NBR adopted in 2011[137] a new Regulation which tightened the rules for banks when setting the maximum amount that the consumer can borrow, in an effort to prevent that consumers reach the point of over-indebtedness. Regulation of the National Bank of Romania no. 17/2012[138] tightened considerably the rules on creditworthiness, especially as regards: categories of income eligible for the lender, differentiated by type of customer and the corresponding adjustment coefficients depending on the degree of certainty and their permanent character; the categories of expenses that are deducted from income, and that are eligible in order to determine the total level of indebtedness, by making sure that at least subsistence expenses and obligations of payment other than credit are not excluded from calculation; calculation of the maximum permissible total level of debt; In substantiation of the maximum permissible total level of debt in case of consumer loans the NBR established precise exchange rate shocks (for example 35.5% euro, 52.6% Swiss Francs , 40.9% US dollar). It also required creditors to analyse the repayment capacity of the clients on the basis of income level that is eligible for the loan, which cannot exceed more than 20% over the prior year. In addition, the NBR established precise rules for loans denominated in foreign currency: the amount of credit for real estate investments may not exceed 85% of the mortgage collateral for loans in RON; in the case of loans denominated in a foreign currency or indexed to the exchange rate of foreign currencies, in case the borrower obtains eligible income denominated or indexed in the currency of the credit, the value of a real estate investment loan is

137 NBR Regulation No. 24 of 28.10.2011 on granting loans to individuals.

138 Regulation of the National Bank of Romania no. 17/2012 concerning certain conditions on lending published in the Official Journal of Romania, Part I, 855, 18.12.2012.

limited to 80% of the mortgage.[139] More detailed rules on the maximum total indebtedness are laid down for special circumstances.[140]

The NBR has been using the instruments at its disposal in order to balance the market's conditions and the general economic backdrop. Its decision to gradually lower the monetary policy rate from 6.5% in March 2010 to 4.25% in September 2013 has contributed to the reduction of the interest rates of the new loans to households, and, consequently, to the improvement of the reimbursement rate of the households' debt service. Moreover, in order to ensure enough buffers for the lenders for the situation when real estate price corrections occur, a Loan-To-Value (LTV) ratio is imposed for consumer loans and mortgage loans. For mortgage loans a distinction is made according to the type of borrowers (hedged vs. unhedged) and according to currency, while for consumer loans the LTV ratio is applied only for foreign exchange denominated loans. In order to reduce debtor vulnerability in case of adverse external shocks (income, currency or interest rate shocks) and therefore increase the resilience of the banks by improving risk management, the Debt-To-Income (DTI) ratio was introduced in 2004. The changes that have occurred since 2000 concerning these two indicators have been determined by the emergence and diversification of the FX rate risk. The more recent revisions have taken place after the publication of the ESRB's recommendations on lending in foreign currencies, as well as the increase of risk occurrence for debtors unhedged against FX rate risk. In 2011, the NBR adopted Regulation 24/2011 on loans to households which explicitly provides the lender's obligation to inform and warn customers on the risks related to foreign exchange borrowing and the consequences of the materialisation of the currency and interest rate risks.

Other NBR envisaged raising sustainability of the debt capacity of consumers. According to the provisions of Regulation No. 24/2011 and Regulation 17/2012, the value of a loan for real estate investments cannot exceed 85% of the value of the mortgage security, in the case of loans granted in RON. If natural persons choose a loan in foreign currency, the value of the loan is limited to 80% of the value of the mortgaged security, provided they earn eligible incomes denominated or indexed according to the currency of the loan. As regards the loan for real estate investments, granted to a natural person who owns incomes in RON, the value of the financing cannot exceed 75% of the value of the mortgage security, in case of loans denominated in euros, or 60% in case of loans denominated in other foreign currency.

2. *Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?*

Law 193/200 on unfair terms by way of the entry into force of the new Code of civil procedure. For the changes in the policies of the National Bank of Romania, see section above.

3. *What are the changes in particular? Focus on consumer credit and mortgage law.*

With the entry into force of the new Code of civil procedure, from October 2013 the revised version of Law no. 193/2000 conferred on consumer associations the right to file a claim against sellers of goods or suppliers of services who use unfair terms in their consumer contracts. Enhanced obligations for

139 Article 16 reads as follows:. *(1) In granting consumer credits denominated in foreign currency or indexed to the exchange rate of a currency, the applicant must have collateral and/or personal information to a minimum of 133% of the loan. (3) If the real estate investment credit granted to individuals covered naturally the currency risk, the financing cannot exceed 75% of the mortgage guarantee for loans denominated in Euro or indexed to the Euro and 60% for loans denominated in other foreign currencies or indexed to the exchange rate of other foreign currencies.(4)* For the purpose of par. (1) - (3), in the case of financing of real estate financial leasing, the limits apply in relation to the value of the financed asset (emphasis added)

140 The maximum total indebtedness is limited to 35% and the maximum indebtedness for a credit for consumption denominated in foreign currency or indexed to the exchange rate of a currency other than that of the eligible income of the borrower cannot exceed 10%.

lending institutions on creditworthiness assessment, and limitation on foreign currency lending were provided in 2012 by the NBR Regulation 17/2012.

4. *When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

The change occurred due to the national policy initiative independent of the crisis (change introduced by the new Code of civil procedure), while the NBR norms were adopted in response to the crisis.

Broader context

XVI. Additional / related problems with impact on consumers' portfolios and indebtedness

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, i.e. with regard to savings?)*

Not relevant.

Annex - Questionnaire

- Preliminary information -

I. The concept of over-indebtedness

1. *Are the terms "indebtedness" and "over-indebtedness" defined in the national legal framework (legislation, jurisprudence)? If yes, how are they defined? If no, are there definitions from other institutions (banks, financial / consumer protection authority, etc.)?*

2. *Is the term "vulnerability" defined in the national legal order with regard to consumers of financial services?*

3. *Is the term "poverty" or "low-income consumer" defined in the national legal order?*

II. Numbers on over-indebtedness

1. *How many consumers / households are considered "indebted" in the country? (since 2000) Please provide absolute numbers.*
   a. *How many consumers have mortgage debt?*
   b. *How many consumers have motor vehicle debt?*
   c. *How many consumers have other debt (credit card, general consumption)?*
   d. *What percentage of those "indebted" consumers / households (a, b, c) is:*
      i. *Single / married*
      ii. *With / without children?*
      iii. *With / without work?*
      iv. *Retired?*
      v. *Low-income consumers?*

2. *How many consumers / households are considered "over-indebted" in the country? (since 2000)*
   a. *How many individual consumers / households are behind with the repayment of (up to 3 months and more than 3 months):*
      i. *General consumption loans*
      ii. *Motor vehicle loans*
      iii. *Student loans*
      iv. *Credit card debt*
      v. *Mortgages / housing loans*
      vi. *Interests*
   b. *How many individual consumers / households have initiated bankruptcy proceedings?*
   c. *How high is the average amount of outstanding debt?*

d. *What percentage of those "over-indebted" consumers / households (a and b)is:*
    i. *Single / married*
    ii. *With / without children?*
    iii. *With / without work?*
    iv. *Retired?*
    v. *Low-income consumers?*

III. Numbers on evictions

1. *How many evictions have there been per year since 2000 (or later if earlier data not available)?*
2. *How many evictions took place because of:*
    a. *Unpaid mortgage instalments?*
    b. *Unpaid monthly rent?*
3. *Who are the persons affected (percentage of young people, families, retirees, unemployed, level of education, low-income consumers)?*

- Relevant legal framework -

IV. Applicable legal framework in the field of consumer credit and mortgage (legislation and national jurisprudence)

1. *Is the CCD 2008/48 implemented into national law?*
2. *Does the national law implementing the CCD 2008/48 include mortgages? Does it go beyond EU legislation in another regard (for example information duties)?*
3. *With regard to the Mortgage Credit Directive Proposal: will there have to be an adjustment of national law if the Proposal is adopted as is? What would be the changes in particular?*
4. *How is the national legal framework with regard to the UCT 93/13?*

V. Enforcement of consumer credit contracts

1. *What are the legal consequences for the loan agreement in case of default on monthly mortgage instalments? What are the lender's and the borrower's rights and obligations?*
2. *What are the requirements to initiate enforcement procedures against the consumer?*
3. *What are the steps of such enforcement procedure?*
4. *Can the consumer raise substantive objections against enforcement?*
    a. *Which ones?*
    b. *What is the legal effect of such objections?*
5. *Does the applicable law allow for an adjustment of contractual terms in the case of "unforeseen/unforeseeable events"?*

a. *How is the term "unforeseen/unforeseeable events" defined?*

b. *If adjustment is possible, what are its legal effects?*

6. *Does the applicable law allow for an adjustment of contractual terms in the case of frustration of contract/purpose?*

7. *Do the banks use private companies that deal with the recovery of debts with the result that legislation on consumer protection doesn't apply anymore?*

VI. National legal framework applicable for over-indebtedness

1. *What are the possibilities for consumers in case they are considered "over-indebted"?*

   a. *Is there the possibility for the consumer to re-organize debt or obtain debt relief?*

      i. *How are the terms re-organization[1] and debt relief[2] defined in the national legal order?*

      ii. *What are the requirements for re-organization and relief?*

      iii. *How many consumers have had debt re-organized?*

      iv. *How many consumers have obtained debt relief?*

   b. *What are the requirements for initiating bankruptcy proceedings for consumers?*

   c. *Is there a possibility for consumers to attain discharge of debt[3] (Restschuldbefreiung) within bankruptcy proceedings?*

      i. *How is discharge defined in the national context? (Is there a definition?)*

      ii. *If discharge is possible, after how many months/years is it possible?*

      iii. *If discharge is possible, what are the requirements for discharge?*

      iv. *How many consumers have obtained from debt discharge?*

   d. *How long do the bankruptcy proceedings last in reality until the consumer is considered debt-free? Is there a legal limit?*

   e. *Are there any other instruments of debt mitigation or debt-restructuring etc. which over-indebted consumers can take recourse to? Please list and elaborate on requirements, legal consequences, and numbers of consumers who have gone through the measures in question.*

2. *Is there a national legal or policy framework for avoiding evictions?*

   a. *Can persons affected stay in their homes during bankruptcy or other proceedings connected to over-indebtedness (ie. debt relief)?*

   b. *Is there a possibility for persons affected to stay in or move again into their homes after the property in question has fallen into the property of the creditor? What are the requirements?*

VII. The regulation of credit bureaus

1. *How many credit bureaus are there in the country?*

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1 Re-organization shall mean the creation of a new budget and establishing priorities for payment.

2 Debt relief shall mean the partial or total forgiveness of debt, or the slowing or stopping of debt growth.

3 Debt discharge shall refer tot he partial or total forgiveness of debt during or after completed bankruptcy proceedings.

2. *Are the credit bureaus public or private? If there are both public and private credit bureaus:*
    a. *How many credit bureaus are public and how many are private?*
    b. *Do the public and private credit bureaus have different functions and / or procedures? Are they concerned with the same data?*
3. *How are credit bureaus compensated?*
4. *How do the credit bureaus collect data?*
5. *In what way do the credit bureaus work together with the data protection agencies in the country? Is there a legal framework?*
6. *What data is collected by credit bureaus?*
7. *Who are the users of credit bureaus?*

- Over-indebtedness -

VIII. Macro-economic risk factors for over-indebtedness

1. *Has there been a housing bubble in the country?*
2. *What is the relation between housing prices and over-indebtedness?*
    a. *How have housing prices developed since 2000 (or later if earlier data not available)?*
    b. *How has the number of over-indebted consumers developed since 2000 (or later if earlier data not available?*
3. *Has there been increased access to mortgage credit? In which way? For example: was access to consumer credit facilitated through legislation? Elaborate. And has access to credit become more restricted since the crisis? Elaborate. If possible provide data.*
4. *What is the relation between employment and over-indebtedness?*
    a. *How many per cent of over-indebted consumers were fully employed / partially employed / self-employed / unemployed consumers at the point in time when*
        i. *the credit contract was signed*
        ii. *over-indebtedness arose?*
    b. *How has the average salary evolved since 2000?*
5. *Non-EURO countries: Did national monetary policy play a role in consumer credit and mortgage agreements? (reference Iceland, Hungary)*
    a. *Are/were foreign currency loans common?*
    b. *What are the foreign currencies in which loan agreements were concluded?*
    c. *Are consumers with foreign-currency loans more indebted than consumers with home-currency loans?*
6. *Are there other macro-economic risk factors for over-indebtedness that can be identified in the national context after the financial crisis?*

IX. "Micro" risk factors for over-indebtedness

1. *What are the most common consumer credit agreements in the country? (What are the reasons for consumers to take a loan – what is the money spent on, acquisition of moveable/immovable property, general consumption?)*

2. *How many credit agreements do consumers conclude on average?*

3. *Was/is the housing market in the country based on rent or ownership?*

4. *How many mortgage agreements were concluded per year since 2007 (or since 2000, if data available)? Please provide absolute numbers AND percentage as of population/home owners/indebted consumers/over-indebted consumers*

5. *How many indebted and over-indebted consumers have credit card debt?*
   a. *How high is this debt?*
   b. *How long does it take consumers on average to repay credit card obligations?*

6. *How many per cent of indebted and over-indebted consumers struggle with the repayment of overdraft facility debt?*
   a. *How high is this debt?*
   b. *How long does it take consumers on average to repay overdraft facility debt?*

7. *Is there a relation between the length of the credit obligation and over-indebtedness?*
   a. *Are there more instances of over-indebtedness when debts arose out of long-term credit agreements?*
   b. *How long are the time periods for which consumers took on credit and mortgage obligations? Is there a difference in data from before and after the crisis?*

8. *What is the average time that passes between the conclusion of a loan agreement and the default of the consumer? Is this average time longer / shorter when the loan period is longer / shorter?*

X. Relation between income and over-indebtedness

1. *How is average income spent in an average household? For example, what proportion of the income is spent on mortgage payments – what proportion of the income is spent on day-to-day needs and other consumption (car, travel)?*

2. *Are low-income consumers subject to other more onerous loan and payment obligations in mortgage agreements?*
   a. *Do lenders consider low-income consumers to be more likely to default and attempt to mitigate this risk through higher interest rates?)*
   b. *Do low-income consumers pay more with regard to the total amount of credit than high-income consumers?*
   c. *Are there other key terms which change according to the income of the borrower?*

- Behaviour of actors -

XI. Irresponsible lending practices

1. *Who was the initiator of the relationship between creditor and borrower (advertising, lender initiative, intermediary, public policy promoting the purchase of houses? Consumer initiative?)*
2. *Was a creditworthiness assessment undertaken before granting the credit?*
    a. *In how many cases were creditworthiness assessments undertaken?*
    b. *Who was the initiator of the creditworthiness assessment?*
    c. *Who undertook the creditworthiness assessment?*
    d. *What were the criteria of the creditworthiness assessment? (empirics)*
    e. *Was a credit bureau involved?*
3. *Is there a legal obligation for a mandatory creditworthiness assessment? How are the criteria for creditworthiness assessment in legal provisions?*
4. *Was credit granted despite a negative outcome of the creditworthiness assessment? If data available: In how many instances was credit refused? What were the reasons given?*
5. *Did the creditor explain to the consumer the consequences of failure to comply with the monthly payment obligations with/without having been asked?*
6. *Did the consumer feel pressured by the lender, for example with regard to signing of the contract, the amount borrowed, or in any other way?*

XII. Irresponsible borrowing practices

1. *Did the consumer read the agreement before signing?*
2. *Did the consumer compare (or have the opportunity to compare) offers before entering into an agreement?*
3. *Did the consumer ask (or have the opportunity to ask) for explanation before signing the agreement?*
4. *How much time did the consumer take before signing the agreement?*
5. *Do consumers make use of the right to withdrawal? (How long is the withdrawal period in the country?)*

- Litigation -

XIII. Issues in litigation

1. *Has there been litigation before national courts challenging the content of mortgage/other loan agreements?*
    a. *What was the applicable law (national, EU, international)? Was the emphasis on contract law or were other fields of law of relevance in the adjudication – if yes, which ones?*

b. *What were the issues in question? (ie: interpretation of unfair terms in – what terms are considered "unfair" within the meaning of UCT 93/13 and the national implementing law?)*

c. *What were the predominant issues (before and after 2008)?*

2. *Who were the plaintiffs? Individuals, organizations, organised groups of consumers, activists, consumer protection or other agencies?*

3. *What is the success rate of legal proceedings brought on behalf of the consumers (borrower) against a financial institution (lender)? What is the success rate of legal proceedings brought on behalf of financial institutions against a consumer-borrower?*

4. *Does the national legal framework allow for litigation in the "public interest" or for the representation of "diffuse" interests? If yes:*

5. *How are those interests defined?*

6. *What are the requirements for such representation?*

7. *In practice, is litigation in "public / diffuse interest" more common than individual litigation?*

8. *Does the national legal framework allow for out-of-court settlement procedures (ADR, consumer protection / financial authorities)?*

9. *Do consumers make use of out-of-court settlement procedures? If yes:*

   a. *Which ones?*

   b. *What is their success rate?*

   c. *What are the issues?*

10. *Are there special bankruptcy courts? What is their role?*

XIV. Impact of the crisis on litigation

1. *Has there been an increase in litigation since the financial crisis (2008)? And how many mortgage agreements were challenged in out-of-court or judicial proceedings before and after the crisis?*

2. *Did the Aziz ruling have an impact on national legislation / legal framework?*

   a. *Are there cases before national courts dealing with issues that also arose in the Aziz case?*

   b. *What was / is considered an unfair contract term in the national court rulings before and after Aziz?*

   c. *Did Aziz have any other impact on national legislation / legal framework (ie. in the field of procedural law)? What are those impacts?*

3. *Is there another case of the CJEU adjudicated after the financial crisis that has had a pivotal impact on the national legal framework? Elaborate.*

- Policy responses & broader context -

XV. National policy responses to over-indebtedness

1. *Has there been a change in national policy / legal framework concerning consumer protection particularly as it relates to financial services after the crisis?*

2. *Which field of law experienced a recent change – bankruptcy law, contract law, tort law, unfair terms, mortgage law, financial supervision?*

3. *What are the changes in particular? Focus on consumer credit and mortgage law. When did the change occur (in compliance with EU legislation, own national policy initiative after the crisis)?*

XVI. Broader context

1. *Are there country-specific phenomena not covered by this questionnaire that had an impact on consumer indebtedness, over-indebtedness, savings, and spendings? (For example: has there been practice of selling risky financial services and products, ie with regard to savings?)*

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