

Opinion of the European Economic and Social Committee on 'Credit and social exclusion in an affluent society'

(2008/C 44/19)

On 16 February 2007, the European Economic and Social Committee, under Rule 29 (2) of its Rules of Procedure, decided to draft an opinion on *Credit and social exclusion in an affluent society*.

The Section for Employment, Social Affairs and Citizenship, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 2 October 2007. The rapporteur was **Mr Pegado Liz**.

At its 439th plenary session, held on 24 and 25 October 2007 (meeting of 25 October 2007), the European Economic and Social Committee adopted the following opinion by 59 votes to 0 with 1 abstentions.

1. Conclusions and recommendations

1.1 In the absence of any Community guidance in this area, the various Member States have developed their own national legal systems for preventing individuals and families from falling into over-indebtedness, processing the cases of those who do, helping them get out of debt and providing them with support.

1.2 Faced with the worrying growth of this phenomenon in recent decades and taking particular account of the European Union's enlargement and the recent deterioration in the situation globally, the EESC — which has been closely following developments in this area for quite some time, as well as the social consequences of over-indebtedness in terms of exclusion, social justice and obstacles to the completion of the internal market — has decided to reopen public debate on this matter with civil society and the other Community institutions. The Committee's intention is to identify and implement Community measures aimed at precisely defining, monitoring and dealing with the problem in all its different aspects — social, economic and legal.

1.3 The diversity of the systems established in the countries that have developed them, not just in Europe but also in the rest of the world, together with the fact that some countries do not have any such systems, is encouraging the development of 'unequal' opportunities, creating social injustice on the one hand, and distortions in the move towards completion of the internal market on the other; all of this warrants urgent, proportionate action by the European Union, for which the necessary legal basis exists in primary law.

1.4 This opinion reviews the main issues raised by the phenomenon of over-indebtedness, weighs up the solutions found at national level, describes the difficulties encountered and errors detected, assesses the overall scale of the problem and reflects on gaps in knowledge and shortcomings in the methods used. The opinion also seeks to identify approaches and pinpoint areas for possible action at Community level.

1.5 The opinion even goes so far as to suggest that a European Indebtedness Observatory be set up to monitor develop-

ments in the phenomenon at European level, providing a forum for dialogue between all the parties concerned, and proposing and coordinating measures to prevent and limit it, then assessing the impact thereof.

1.6 The Committee is aware, however, that coordinating steps of this nature and scope can only be achieved if the Commission, European Parliament and Council — in close dialogue with organised civil society, representing the bulk of those concerned by the issue (families, workers, consumers, financial institutions, etc.) — decide to make this a priority for action.

1.7 Recent indications of the Commission's thinking on this matter are therefore to be welcomed and it is strongly recommended that the necessary follow-up be given in terms of basic research, consultations and legislative and other relevant proposals, starting with the publication of a Green Paper defining and identifying the terms of the issue and giving a voice to all the parties concerned, by means of extensive public consultation.

1.8 Furthermore, the EESC calls on the European Parliament and the Council to take on board the major concerns that this opinion attempts to address on behalf of civil society and make them a priority in their respective political agendas.

2. Introduction

2.1 Credit has undeniably enabled people in Europe to improve their quality of life and access essential goods and services which would otherwise have been beyond their reach or only affordable after a considerable length of time, such as their own homes or means of transport. Nevertheless, if the conditions under which credit is provided are not sustainable — if serious employment problems arise, the monthly burden of debt exceeds a reasonable proportion of available monthly income, too many loans have been taken out or there are no savings to help tide people over times when they have no income — credit can lead to situations of over-indebtedness.

2.2 In fact, the problem of over-indebtedness and its social consequences is not new. Its origins might even be glimpsed as far back as times of Classical Antiquity, more specifically the agrarian crisis suffered by Greece in the VIth century BC and Solon's measures (594/593 BC), first of all to write off the debts of farming small-holders who had been reduced to slavery and sold off, and then to free these people and reintegrate them into Athenian society and productive life as free citizens ⁽¹⁾.

2.3 However, there is no doubt that nowadays this phenomenon is becoming increasingly widespread and assuming worrying proportions. People are becoming more aware of it as a social problem in a society hallmarked by sharp contrasts, where discrepancies continue to grow and solidarity is much less in evidence.

2.4 It is against this background that the question of banking exclusion is to be seen, denoting the marginalisation of those who, for various reasons, are prevented from having access to basic financial services ⁽²⁾.

2.5 This opinion seeks to pinpoint the main causes of this problem, its scale, the remedies most frequently brought to bear and the reasons for seeking a solution at Community level.

3. Scale of the problem

3.1 Social exclusion and banking exclusion

3.1.1 According to the Eurobarometer Report of February 2007 ⁽³⁾, around 25 % of Europeans feel that they are at risk of sliding into poverty and 62 % believe that this is something that could happen to anyone, at any time of life.

3.1.2 Data from the European Commission's 2007 Joint Report on Social Protection and Social Inclusion indicate that in 2004, 16 % of the EU15 population lived below the poverty line, which is set at 60 % of the average income of each country ⁽⁴⁾.

⁽¹⁾ As referred to by Aristotle in his treatise on the 'Constitution of Athens' (in part 6 in particular, which states: 'As soon as he was at the head of affairs, Solon liberated the people once and for all, by prohibiting all loans on the security of the debtor's person: and in addition he made laws by which he cancelled all debts, public and private. This measure is commonly called the *Seisachtheia*, since thereby the people had their loads removed from them' [translated by Sir Frederick G. Kenyon] and whose 'identity' of situations will have influenced the fascinating contribution by Udo Reifner entitled 'Renting a slave — European Contract Law in the Credit Society' at the conference on private law and the various cultures of Europe, held at the University of Helsinki on 27 August 2006. Note that imprisonment for debtors still applied in most European countries until the XXth century.

⁽²⁾ On this subject, see the recent contribution by Georges Gloukoviezzoff entitled 'From Financial Exclusion to Overindebtedness: The Paradox of Difficulties for People on Low Incomes?' in 'New Frontiers in Banking Services', Luisa Anferloni, Maria Debora Braga and Emanuele Maria Carluccio, Springer.

⁽³⁾ Cf. Special Eurobarometer 273, *European Social Reality*, 2007.

⁽⁴⁾ 2007 Joint Report on Social Protection and Social Inclusion, adopted by the Council on 22.2.2007 (COM(2007) 13 final of 19.1.2007).

3.1.3 In qualitative terms, poverty corresponds to a lack or inadequacy of material resources for meeting the vital needs of an individual; this is the most visible aspect of social exclusion, which pushes the individual back out to the margins of society, thus generating feelings of rejection and self-exclusion.

3.1.4 The extent and form of social exclusion depend, in each country, on a number of variables such as the social security system, the way the labour market operates, the justice system and informal solidarity networks. Immigrants, ethnic minorities, the elderly, children under 15, people on low incomes with few educational qualifications, people with disabilities and the unemployed are the most vulnerable to poverty and social exclusion.

3.1.5 In most European countries, consumer trends indicate a relative fall in spending on foodstuffs, drink, tobacco, clothing and footwear, and a relative rise in expenditure on housing, transport and communication, health services, culture and other goods and services such as health care, tourism and hotel and catering services ⁽⁵⁾.

3.1.5.1 This new distribution in household spending tends to be reflected in the use of credit. Consumer credit in the broad sense of the term, which includes the purchase of both consumer goods and housing, is nowadays closely linked to new patterns of consumption and closely follows the ups and downs of developments in these patterns. Thus, the increased share of spending on domestic utilities, transport and travel ⁽⁶⁾ frequently involves payment by credit.

3.1.5.2 Another factor encouraging the increase in consumer credit is the fact that a) the latter has lost its negative connotations of poverty and guilt in respect of the way that people lead their lives or manage their businesses, mainly in countries where people are predominantly catholic, as compared to protestant, in upbringing, and b) it has become quite common, especially in the big cities. Pushy, systematic advertising by financial bodies to attract new clients is encouraging more people to take out loans. In addition, consumer credit confers status and makes it easier to camouflage people's social background, allowing them to adopt a lifestyle characteristic of a class higher than their own. For many families, credit is a common way of managing a household budget (especially using credit cards), where the risks are known; however not enough information is provided on these risks or on the effective solutions to the problem, and even the extent of the risks has not yet been properly quantified.

⁽⁵⁾ Cf. Eurostat — *Les nouveaux consommateurs* (The new consumers), Larrousse 1998.

⁽⁶⁾ Whilst not overlooking the considerable differences between these three, even in terms of fundamental rights.

3.1.6 These determining social and cultural factors are also underpinned by economic and social ones such as the sharp drop in interest rates over last decade, the fact that people have a lower propensity to save and persistently low unemployment rates, all combined with economic growth (despite the crisis of the late nineties which nonetheless did not assume the same proportions as previous such crises). On top of this has come deregulation, which targeted the whole of the credit market from the late seventies and early eighties onwards ⁽⁷⁾, triggering a rapid expansion in the scale and number of credit providers, including some not subject to monitoring and financial supervision, together with an increase in competition between them, all leading to a depersonalisation of the bank-customer relationship.

3.1.7 These factors together have all meant that European society is becoming increasingly dependent on credit being granted for people's key needs to be met. The growing extent of indebtedness in most Member States clearly illustrates this fact ⁽⁸⁾.

3.1.8 If credit is taken out on a sustainable basis — where there are no serious employment problems, where the share of monthly debt payments as part of monthly disposable income is not excessive, where the number of loans taken out is not high and where there are some savings to tide people over occasional periods without income — it can help people improve their quality of life and allow them access to essential goods and services which they could not otherwise afford, or only after a long time, such as housing and private cars.

3.1.9 Nevertheless, the prospect of something going wrong in private or family life, causing financial commitments not to be met at a particular moment, is a risk run by everyone signing a credit contract. Thus, normal, controlled indebtedness can for a variety of reasons become uncontrolled over-indebtedness.

3.2 Concept and measure of over-indebtedness

3.2.1 Over-indebtedness refers to situations where the debtor is unable to pay all his debts on a long-term basis, or where there is a serious risk that this might be the case when the debts fall due ⁽⁹⁾. Nevertheless, the precise terms of this concept vary

⁽⁷⁾ This only occurred in the new accession countries in the 1990s.

⁽⁸⁾ Cf. The data set out in the Bank of France Bulletin No 144, December 2005. URL: http://www.banque-france.fr/fr/publications/telechar/bulletin/etu144_1.pdf;

⁽⁹⁾ The exemplary definition by Udo REIFNER states: 'Over indebtedness means being objectively unable to pay; more precisely, the relevant income after deduction of living expenses is no longer sufficient to meet the repayment of debts when they fall due' (in 'Consumer Lending and Over Indebtedness among German Households').

considerably from country to country in the EU, and its definition at European level is still lacking ⁽¹⁰⁾. The recent European Commission initiative to commission a study on this subject is therefore to be welcomed ⁽¹¹⁾.

3.2.2 Not only is the concept in itself ambiguous and its definition not straightforward, there are also several different ways to measure over-indebtedness. Thus, in a study commissioned by the European Commission ⁽¹²⁾, there were three different formulas or models devised for measuring over-indebtedness: the administrative model ⁽¹³⁾, subjective model ⁽¹⁴⁾ and objective model ⁽¹⁵⁾.

3.2.3 One of the main difficulties in assessing the scale of over-indebtedness in Europe relates to the lack of reliable statistics, and the fact that is impossible to draw comparisons with existing data, given the different methods, concepts and time periods applied. This is one area to which the Commission

⁽¹⁰⁾ The concept of over-indebtedness underlying the highly diverse legislative initiatives is above all derived from the legal rules setting the access conditions to any debt restructuring procedure, be it extrajudicial or judicial. Thus, for example, French law allows access to *debtors acting in good faith who are clearly unable to meet the whole of their professional debts due or falling due* (Article L.331-2 of the *Code de la Consommation*). Likewise, Finnish law (1993) considers *debtors to be over-indebted or insolvent when they are not in a position to pay their debts when they fall due, where this is a permanent situation and not only accidental or temporary*. Other countries, however, limit their definition to a series of procedural and personal requirements for access to schemes for dealing with over-indebtedness, without risking a definition thereof. Such is the situation in Belgian law (Law of 5 July 1998, amended by the Law of 19 April 2002) and North American law (*Bankruptcy Code*, revised in 2005).

⁽¹¹⁾ 'Common operational European definition of over-indebtedness (Contract No VC/2006/0308, of 19.12.2006)', financed by the European Commission, DG Employment, Social Affairs and Equal Opportunities and conducted by the European Savings Observatory.

⁽¹²⁾ 'Study of the Problem of Consumer Indebtedness: Statistical Aspects (contract No B5-1000/00/000197)', carried out by OCR Macro for DG SANCO.

⁽¹³⁾ The *administrative model*: the measure of over-indebtedness is given by official statistics referring to formal procedures for dealing with such cases. This option leaves out a part of the actual situation, since not all debtors in difficulty make use of official, legal proceedings. Moreover, the variety of legal solutions in place in the different countries of Europe make it impossible to draw exact comparisons between them.

⁽¹⁴⁾ The *subjective model* is based on individuals' or families' perceptions of their financial solvency. Families consider themselves to be over-indebted when they state that they have major difficulties in paying all their debts or are already unable to do so. The criterion in this model is also difficult to apply in practice, compromising the comparability of data. An increasing number of people are drawing attention to the fact that people's judgement is clouded by *overoptimism, underestimation of risk and hyperbolic discount* when assessing financial sustainability and deciding about whether or not to use credit to make payments.

⁽¹⁵⁾ The *objective model* uses the economic and financial situation of households as a measure of inability to pay, i.e. the relation between total debt and net salary or between total debt and net salary and assets together. This is the formula generally used by financial institutions and also by some national legal systems. Although this is not without its problems, such as knowing to what extent the debtor's behaviour, honesty and good faith should have an influence on access to a system for settling and writing off debts, this is one criterion which enables comparisons to be drawn and which may provide a basis for devising a common legal concept of over-indebtedness.

should devote more attention, carrying out the studies needed to obtain and process reliable, comparative data.

4. Main causes of over-indebtedness

4.1 The numerous sociological studies carried out in the various Member States have pinpointed the following main causes of over-indebtedness:

- a) unemployment and deteriorating work conditions;
- b) changes in the structure of households as a consequence of, for example, divorce, death of a spouse, unplanned child, unexpected support needed for older people or invalids, illness or accident;
- c) failed attempt at self-employment, collapse of a small family business for which personal guarantees have been put up;
- d) advertising and marketing campaigns pushing people to consume, offering easy credit and encouraging people to gamble, play the stock market and boost their status;
- e) higher interest rates, the negative effect of which is felt above all in long-term loans, such as mortgages;
- f) bad household budget management;
- g) deliberate concealment by customers of information that would enable financial institutions to assess their solvency;
- h) excessive use of credit cards, revolving credit and types of personal credit extended by financial companies, with high interest rates;
- i) credit obtained on the informal market, above all by people with low incomes, at usurious interest rates;
- j) credit used to pay for other loans, creating a snowball effect;
- k) the fact that socially isolated disabled people and people with limited cognitive skills can easily fall prey to aggressive lenders;
- l) The unwillingness of certain financial institutions to renegotiate debt repayment with less well-off consumers who find themselves in financial difficulties.

Sociological analysis of the phenomenon thus indicates that there is a predominance of passive causes, although it should be pointed out that in some countries, bad financial management has also been recognised as being at the root of the problem ⁽¹⁶⁾. This suggests that individuals encounter difficulties in managing their budgets in a careful, sustainable fashion ⁽¹⁷⁾.

4.2 Financial exclusion is normally reflected in difficult or denied access to the basic financial services market, namely for opening a current account, using electronic means of payment, being able to make bank transfers and taking out insurance for credit protection.

4.3 Such financial exclusion includes, *a fortiori*, difficult or denied access to low-cost loans enabling the purchase of essential goods and services for a family household (house, domestic appliances, transport and education), a self-employment start-up, or the management of a small one-person or family business.

4.4 Nowadays, access to a bank account, to certain forms of credit and electronic transfers between accounts is an essential pre-condition for accessing key goods and services. Employment, a small business, a house to live in, house fittings, transport, information and even food, clothing and leisure all require access to credit and banks — the latter thus bearing a special social responsibility for providing something almost akin to a public service.

4.5 It is here that the line becomes blurred between a growing and increasingly impoverished middle class and those who are definitively excluded, homeless, beggars, and those dependent on charity. It is precisely at this threshold of poverty that the prevention of over-indebtedness makes sense, together with ways to deal with and recover from it, and also to prevent those who are socially and economically surviving or recoverable from falling irreparably into a cycle of poverty and social exclusion.

5. Prevention of over-indebtedness and ways of dealing with it

5.1 Prevention

In national systems, the emphasis tends to be on measures to prevent over-indebtedness, including:

⁽¹⁶⁾ Bank of France figures for 2004 estimate that 73 % of over-indebtedness files submitted to the Commissions for Over-indebtedness are rooted in passive causes.

⁽¹⁷⁾ On the factors affecting over-indebtedness, see the EESC Information Report of 26.6.2000, entitled 'Household over-indebtedness' (rapporteur: Mr Ataíde Ferreira) in which the subject was examined extensively.

- a) **More complete and widely available information** on financial services in general, their costs and the way in which they operate.
- b) **Financial education**, included from an early stage in school curricula and other areas of education and training, such as *lifelong learning processes* reflecting the needs and skills of the individuals it aims to assist, which can be varied throughout life cycles and in keeping with the culture, values system, socio-demographic and economic characteristics, consumer standards and indebtedness of those concerned. It is worth highlighting the fact that in some Member States, the 'media' and in particular television, with its public service remit, have — with the cooperation of consumers' associations and the financial institutions themselves — broadcast programmes to raise awareness of the issues of credit and indebtedness, often at peak viewing hours. Moreover, adult education structures, like those provided in some countries by family education centres, should be used.
- c) **The creation or extension of financial advice networks** that help people to a) manage their budget in a balanced way, b) choose the best options for financing their purchases ensuring that the balance of information is not skewed towards the financial institutions and c) draw up sustainable repayment plans by means of simulations before credit is granted.
- d) **Incentives to save** (such as tax breaks and social and educational incentives), which would be a household's first line of defence when faced with financial difficulties. Such incentives could also act as a counterbalance to aggressive publicity advertising credit.
- e) **The use of credit scoring systems**, whether these are credit institutions' own systems or contracted out to specialist companies, in order to assess clients' credit risks. This enables the lender to gauge the risk of insolvency by assessing a whole series of variables and setting objective limits for individual and household debt ⁽¹⁸⁾.
- f) **The guarantee of proper pensions**, early retirement provision and other social benefits for people outside the labour market, incorporated into effective social security schemes

⁽¹⁸⁾ Whilst this is an important risk-management instrument for financial institutions, there is a need for greater transparency in the content of scoring systems and for these to be combined with subjective means of analysis so that an accurate, realistic assessment can be made of debtors' ability to repay and so that decisions are not based solely on automated models. There is also a need for the variables of the mathematical model to be monitored by the relevant public authorities. In addition, consideration should be given to the possibility of giving debtors access to their credit reports, as happens in countries such as the USA and the United Kingdom, so that individuals can see how to improve their credit rating.

by the public authorities, as an essential condition for ensuring that those unable to access private **pension funds** are not excluded from society ⁽¹⁹⁾.

- g) **Access to basic insurance** for securing credit as a means of protecting against financial risk ⁽²⁰⁾.
- h) **Social credit, microcredit and affordable credit**

Schemes such as microcredit, credit unions, savings banks, the German and Dutch social funds, post office banking and social credit are, alongside other schemes starting up in the Member States, examples to bear in mind for people at risk of exclusion who are seeking affordable credit. Microcredit, for example, has helped finance small businesses and self-employment, enabling some of the unemployed to re-enter the labour market and start some economic activity again. It is recommended that the financial institutions provide specialist assistance (in management, accounting, commerce, etc.) to help the beneficiaries of microcredit to manage their activity, a practice already being adopted in a number of cases ⁽²¹⁾.

- i) **Responsible lending**, which requires credit institutions to pay greater attention to the needs and situations of their individual borrowers, to find the financial instrument most appropriate to each one's circumstances, and even to deny further credit where there is imminent risk of over-indebtedness ⁽²²⁾.

⁽¹⁹⁾ Furthermore, it is essential to prevent financial practices which seek to misuse the pensions of the most dependent members of society by using pensions as guarantees for loans that are disproportionately high in relation to their means to repay them. In Brazil, for example, a type of credit targeting the elderly, known as 'crédito consignado' [a loan granted against income], was set up in 2004. This special type of credit is deducted from pensions at source, up to a maximum of 30 % of the pension's total value. The fact that the interest rates offered are lower than those available on the market does enable pensioners to access credit; however this appears to be causing financial difficulties for people on the lowest pensions, causing them to default on other repayments and depriving them of sufficient resources to meet their basic needs.

⁽²⁰⁾ Insurance plays an ambivalent role in relation to social exclusion. Compulsory life insurance can exclude people with health problems from the credit market, but a life insurance policy can also prevent someone who unexpectedly falls ill from losing their insured assets and thus sliding into poverty and exclusion.

⁽²¹⁾ In France and Belgium, consumer microcredit (known as social microcredit) is being used in an experimental scheme by a number of banking networks, in partnership with relevant associations. To date, the experiment has been reasonably successful but it is still too early to be able to make a definitive assessment. To be highlighted in the case of Belgium is the experience of Credal, a Belgian social credit cooperative, created under a public/private partnership between the Walloon Regional government and a number of financial institutions.

⁽²²⁾ See for example the 'Protocollo sullo sviluppo sostenibile e compatibile del sistema bancario' signed on 16 June 2004 in Rome between the 'Associazione Bancaria Italiana' and the 'Federazione Autonoma Lavoratori del Credito e del Risparmio Italiani (Falcri)', the 'Federazione Italiana Bancari e Assicurativi (Fiba-Cisl)', the 'Federazione Italiana Sindacale Lavoratori Assicurazioni e Credito (Fisac-Cgil)', the 'Uil Credito, Esattorie e Assicurazioni (Uil C.A.)'.

j) **Credit history files**

The use of databases containing either customers' entire financial histories (positive credit history files) or just their repayment problems (negative credit history files) helps credit institutions ascertain customers' levels of indebtedness and provide a sounder basis on which to grant loans. This is despite the acknowledged risks, in particular relating to positive credit history files, in terms of privacy protection, and the fact that such files provide no help where there is passive indebtedness, a) since it is impossible to predict what might cause similar situations in the future and b) because they take no account of other, non-financial debts (for example, debts relating to essential services and the payment of taxes).

- k) **Self- and co-regulation**, leading to the establishment of **Codes of Conduct** by financial bodies, specifically in partnership with consumer protection organisations, can help prevent some abusive practices and instil a more socially responsible approach on the part of credit institutions. This type of measure is also useful for improving the monitoring of debt collection agencies' activities, helping to regulate the way in which debtors are dealt with, as a complement to a rigorous, effectively implemented legislative framework.

l) **Prevention of abusive credit practices**

Some national authorities, consumer protection organisations, other NGOs and the credit institutions themselves have agreed rules and procedures to prevent the use of a number of predatory and usurious practices that threaten the most disadvantaged members of society. These practices include, for example, extremely high interest rates on credit granted over the telephone or mobile telephone, credit contracts, of which the customer is unaware, tied to contracts for a specific purchase, sale, or the provision of services, the granting of credit to acquire stock market shares, sometimes involving shares issued by the same bank as the one granting the loan, draconian penalty clauses, credit cards and store cards providing easy access to credit, the demand for surety and at the same time personal guarantees (collateral) for low-value consumer credit contracts, incomplete or not fully accurate information and advertising targeting young people. In addition to the beneficial aspects of responsible credit provision, measures of this nature help

reduce distortions in competition on the market and promote social responsibility amongst credit institutions.

m) **Monitoring advertisements for credit**

Although advertising is a legitimate strategy for promoting financial products, the way in which these products are advertised calls for close monitoring by the public authorities. The content, vehicles and techniques of advertising should be subject to strict, harmonised regulation that does not leave consumers with the idea that credit is risk-free, easily accessible and without cost. Schemes for self- and co-regulation and good business practice should also be encouraged in this field. These schemes should give borrowers complete clarity as to the conditions of the loan and place a particular responsibility on lenders towards people who, because of mental impairment, are not in a position to appreciate the consequences of entering into a debt agreement.

5.2 *Dealing with debtors and debt recovery*

The two most common models of dealing with insolvent debtors and of recovering debt are:

5.2.1 **The fresh start model**, which originated in North America and has been adopted in some European countries, is based on the principles of immediately liquidating a debtor's non-exempt assets and writing off unpaid debts, except those that cannot legally be written off. This model is based on the concept of limited debtor liability, on sharing risk with the creditors, on the need to return the debtor as quickly as possible to economic activity and consumption, and on clearly not stigmatising the bankrupt individual ⁽²³⁾.

5.2.2 **The re-education model**, used in some European countries, is based on the idea that the debtor has failed and should be helped, but not simply be exonerated of the duty to fulfil his or her obligations (*pacta sunt servanda*). This model, based on the idea of the 'guilt' of the bankrupt individual — whether the failure results from a lack of foresight or from plain negligence — centres on the renegotiation of debts with the creditors, with the aim of securing agreement on a general repayment plan. This plan can be negotiated through the courts or extrajudicially; what is important is the role played by the debt advisory and mediation services ⁽²⁴⁾.

⁽²³⁾ For a detailed critical description of this model, see the work of Karen Gross, who is well-known in Europe, in particular 'Failure and Forgiveness. Rebalancing the bankruptcy system', New Haven, Yale University Press (1997).

⁽²⁴⁾ Some legal systems, such as those in France and Belgium, have reformed their laws on managing the over-indebtedness of individuals to incorporate alternative solutions based on asset liquidation. In the most serious cases, where the repayment plan does not present a solution, liquidation is possible, followed by debt forgiveness. Nevertheless, unlike in US law, debt forgiveness is never immediate. The debtor must complete a probationary period, during which he must set aside part of his income to pay off the outstanding debt. Only then, and only if the debtor has demonstrated honest behaviour and good faith, can the debt be written off. Exceptionally, in France, a debt can be written off as soon as court proceedings begin, if the judge considers that there is no hope of the individual's situation improving, even though this procedure has been little used to date.

6. Why a Community-level approach is needed

6.1 Background

6.1.1 This is not the first time that the issue of over-indebtedness has been addressed at Community level or even from a Community perspective, within the EU institutions. On 13 July 1992, in its resolution on future priorities for the development of a consumer protection policy, the Council considered studying over-indebtedness as a priority for the first time. Since then, however, although the phenomenon of over-indebtedness has been becoming increasingly serious in the various Member States, resulting in most of them adopting specific legislative and administrative measures to deal with it, the question of a Community-level approach has been all but forgotten.

In May 1999, the EESC decided to reopen the debate on the issue, first drawing up an information report on 'Household over-indebtedness', followed by an own-initiative opinion on the same subject in 2002; the reader is referred to the comments and recommendations contained therein ⁽²⁵⁾.

6.1.2 In fact, while the Committee was drawing up these documents, the Luxembourg Consumer Affairs Council of 13 April 2000 took a fresh look at the issue and drew the Commission's and Member States' attention to the need for Community harmonisation in this field. Following this, the Council adopted its Resolution on consumer credit and indebtedness ⁽²⁶⁾, in which, noting the rapid growth of the phenomenon, it urged the Commission to take steps to plug the gaps in information on the real extent of over-indebtedness in Europe and to examine thoroughly the possibility of harmonising measures to prevent and deal with cases of over-indebtedness ⁽²⁷⁾.

6.1.3 It should be pointed out that the Commission has not to date fulfilled its brief from the Council. It only mentioned the issue of responsible credit provision ⁽²⁸⁾ briefly in its initial proposal to review the Consumer Credit Directive (2002) ⁽²⁹⁾. These references disappeared, however, from its final version (2005) ⁽³⁰⁾, confirmed under the German presidency ⁽³¹⁾. This situation suggests that in the field of consumer credit, it will be difficult for the Commission ever to adopt any new measures to prevent or even deal with over-indebtedness ⁽³²⁾.

⁽²⁵⁾ These papers were both drawn up by the former Committee member Manuel Ataide Ferreira.

⁽²⁶⁾ Resolution of 26 November 2001, in OJ C 364, 20 December 2001.

⁽²⁷⁾ The minutes of this Consumer Affairs Council of 26 November 2001 state that Ministers considered, amongst other observations and recommendations, that '*divergences as regards both the preventive and the social, legal and economic treatment of over-indebtedness in the Member States could therefore give rise to considerable disparities both between European consumers and between credit-providers*' and thus that '*(...) consideration could be given at Community level to complementing the measures to promote the development of cross-frontier credit with measures to prevent over-indebtedness throughout the one credit cycle*'.

⁽²⁸⁾ In terms that are highly debateable, as the EESC stated in its opinion on that proposal (CES 918/2003, 17 July 2003): rapporteur, Mr Pegado Liz. See also '*La prevención del sobreendeudamiento en la propuesta de directiva sobre el crédito e los consumidores*' [*Preventing overindebtedness in the proposed directive on credit and consumers*] by Manuel Angel, López Sánchez, in '*Liber Amicorum Jean Calais Auloy*', p. 62.

⁽²⁹⁾ COM(2002) 443 final, 11 September 2002.

⁽³⁰⁾ COM(2005) 483 final/2, 23 November 2005.

⁽³¹⁾ It is, however, worth highlighting some initiatives for public debate promoted by different Community institutions, including the Commission, on the issue. These include: a public hearing held in Stockholm with the support of the Swedish presidency on 18 June 2000; a major conference held on 2 July 2001 in cooperation with the *Consiglio Nazionale dei Consumatori e degli Utenti* [Italian National Council for Consumers and Users] (CNCU) on '*Competition rules in the EU and banking systems in conflict*', at which the Director at the Financial Services Directorate, DG SANCO, presented the approaches adopted in the proposal for the new consumer credit directive and over-indebtedness problems at Community level; on 4 July 2001, DG SANCO organised a hearing of government experts in Brussels to discuss proposed changes to the consumer credit directive, at which various aspects of preventing over-indebtedness were highlighted; during the Belgian presidency a major seminar was held in Charleroi on 13 and 14 November 2001 on the theme of '*Consumer credit and Community harmonisation*', at which the Belgian Minister for the Economy and Scientific Research in particular raised the social and economic aspects of the issue, stressing the link with the development of financial services and cross-border trade in the internal market. A European Commission expert also gave a presentation on the broad guidelines for the review of the consumer credit directive, in which certain concerns about consumer information relate to preventing over-indebtedness; and the '*Conference on consumer over-indebtedness: protection mechanisms in Europe*', promoted by the PSOE [Spanish Socialist Workers' Party] and by the Socialist Group in the EP, in Madrid on 29 November 2002.

⁽³²⁾ Curiously, in other texts such as the Commission Proposal on the SEPA (*Single Euro Payments Area*), a number of concerns are expressed with regard to preventing over-indebtedness.

6.1.4 Recent references in some Commission documents, albeit few and far between, and even in statements by the Commission President, do appear, however, to express a possible shift towards paying closer attention to the phenomenon ⁽³³⁾.

6.1.5 In view of its importance, particular reference should be made to the Council of Europe Resolution adopted by European Ministers of Justice on 8 April 2005, on '*seeking legal solutions to debt problems in a credit society*' ⁽³⁴⁾, which, whilst expressing concern at the '*easy access to credit that can in some cases result in the over-indebtedness of households creating social exclusion of individuals and their families*', clearly opens the way to preparing '*an appropriate instrument defining legislative and administrative measures, and proposing practical remedies*' ⁽³⁵⁾.

6.1.6 Furthermore, renewed awareness of the problem appears to have been stimulated by recent academic studies ⁽³⁶⁾ and others specifically requested by the Commission ⁽³⁷⁾, having been the subject of recent public remarks by certain Heads of State and ministers from some Member States ⁽³⁸⁾.

6.2 The possibilities, need and opportunity for Community-level action

6.2.1 The EESC has long argued and is now again stating that Community-level action in this field is not only possible and desirable, but is actually necessary and even urgent.

6.2.2 The EESC is not unaware that, under the terms of the Treaty and following the failure to adopt the constitutional text ⁽³⁹⁾, the purely social aspects of over-indebtedness as a cause of social exclusion do not fall within the EU's specific remit.

6.2.2.1 Nevertheless, various provisions of the Treaties on European Union and establishing the European Community stipulate both shared powers and actions and measures to back up and encourage Member States' policies in this area ⁽⁴⁰⁾, which it is up to the Commission to secure and develop.

6.2.2.2 It should be added that some areas for potential action at Community level are now covered by the third pillar, coming under cooperation in judicial matters ⁽⁴¹⁾.

⁽³³⁾ See in particular, the Eurobarometer survey published late 2006, the Communication entitled '*A Citizens' agenda*' adopted by the Council in July 2006 and the Commission Communication on the Joint Report on Social Protection and Social Inclusion 2007 (COM(2007) 13 final, of 19 January 2007).

⁽³⁴⁾ Adopted at the Council of Europe's 26th Conference of European Ministers of Justice, held in Helsinki on 7 and 8 April 2005.

⁽³⁵⁾ As a follow-up to the well-drafted '*Report on Legal Solutions to Debt Problems in Credit Societies*' by the Council of Europe's Bureau of the European Committee on Legal Co-operation, of 11 October 2005 (CDCJ-BU(2005) 11 rev.).

⁽³⁶⁾ The academic world appears to be particularly interested in the issue of consumer credit and over-indebtedness, as demonstrated by the recent scientific meeting held in Berlin from 25 to 28 July by the Law and Society Association, which was attended by a group of researchers from Europe, America (both North and South), Asia and Australia, who discussed, in the course of 8 sessions, various aspects relating to these matters.

⁽³⁷⁾ See '*Consumer Over-indebtedness and Consumer Law in the European Union*', Udo Reifner, Johanna Kiesilainen, Nic Huls and Helga Springener (Contract No. B5-1000/02/000353, for DG SANCO Sept. 2003); '*Study of the problem of Consumer Indebtedness: Statistical Aspects*', ORC Macro (Contract No B5-1000/00/000197, for DG SANCO, 2001); '*Credit Consumption and Debt Accumulation among Low Income Consumers: Key consequences and Intervention Strategies*' Deirdre O'Loughlin (Nov. 2006); '*Exclusion and its links to finance: banking exclusion of individuals*' Report produced by the Centre Walras, Georges Gloukoviezoff; '*EC Consumer Law Compendium: Comparative Analysis*', 2006, (contract No 17.020100/04/389299) drawn up by Hans Schulte-Nölke, of the University of Bielefeld for the European Commission; '*Financial education & better access to adequate financial services*', carried out by ASB Schuldnerberatungen (Austria), in cooperation with the GP-Forschungsgruppe: Institut für Grundlagen-und Programmforschung (Germany), the Association for the Promotion of Financial Education SKEF (Poland) and L' Observatoire du Crédit et de l'Endettement (Belgium) — the project was co-financed by DG Employment and Social Affairs (September 2005-September 2007).

⁽³⁸⁾ See, for example, recent speeches by Tony Blair, Stephen Timms and Ruth Kelly in September 2006.

⁽³⁹⁾ In fact, Article I(3) of the draft Constitutional Treaty states that one of the Union's aims shall be to '*combat social exclusion and discrimination, and ... promote social justice and protection ...*'.

⁽⁴⁰⁾ Particular emphasis should be placed on the concepts set out in Articles 2 and 34 of the EU Treaty and Articles 2, 3, 136, 137 and 153 of the Treaty of Rome, as amended by the Treaty of Amsterdam. Attention should also be paid to the integrated open method of coordination (OMC) introduced in 2006, aimed at enhancing the EU's capacity to support Member States' efforts to ensure greater social cohesion in Europe.

⁽⁴¹⁾ See Articles 65 and 67 of the Treaty and the already extensive role of measures adopted to define a European judicial area.

6.2.2.3 Lastly, it is the completion of the internal market itself, now unequivocally geared to the general public and consumers ⁽⁴²⁾, which requires and warrants the harmonisation of certain aspects relating to over-indebtedness, and its social repercussions, prevention and management at Community level, as a means of preventing distortions in competition and obstacles to the smooth operation of the market.

6.3 Main areas of activity at Community level

6.3.1 A single concept of over-indebtedness

6.3.1.1 Steps to achieve harmonisation should primarily involve defining the concept and qualitative and quantitative parameters of the phenomenon in order to secure full information and proper observation of the underlying social circumstances, in identical terms throughout Europe — and ideally, throughout the world — based on the compilation and processing of comparable statistical data, which will help define an economic framework for quantifying this data.

6.3.1.2 On the basis of this conceptual and methodological definition, the Commission should sponsor a study covering the entire Community area, contributing to an assessment of the economic and social aspects of over-indebtedness ⁽⁴³⁾.

6.3.2 Prevention and containment

6.3.2.1 The Commission should also draw up independent, harmonised legislation for measures that plan for, prevent and limit the impact of this phenomenon.

There should, in particular, be laws on:

- a) exhaustive pre-contractual and contractual information and after-sales follow-up;

⁽⁴²⁾ Clearly demonstrated in the excellent Interim report to the 2007 Spring European Council, the Commission communication entitled 'A single market for citizens' (COM(2007) 60 final, 21 February 2007), and in various speeches and interviews given recently by the Commission President himself.

⁽⁴³⁾ Data on the situation in Europe are somewhat out of date, referring to the study published in 2001 by OCR Macro, as mentioned above. Nevertheless, several Member States acknowledge that the number of families affected by over-indebtedness has increased significantly in recent years. Data on the situation in Germany indicate that in 1989, only 3,5 % of families experienced serious financial difficulties, whilst in 2005, 8,1 % of German households were over-indebted (In France, the number of cases brought before the French Commissions for Over-indebtedness increased at a rate of 6 % per year between 2002 and 2006, when 866 213 cases were heard. In Scotland, also in 2004, more than 3 000 cases of insolvency were declared. In Sweden, despite the fact that the annual economic growth rate is one of the highest in the EU, the number of over-indebtedness cases rose in 2005 by 13,6 % compared to 2004 and by 30,7 % compared to 2003. The exception would appear to be Belgium, where a well-designed, well-implemented system appears to be yielding results, with the assistance of recent changes to legislation (the Law and Royal Decree of 1 April 2007, amending the Law of 24 March 2003 and the Royal Decree of 7 September 2003, on basic banking services). In the USA in 2005, more than 1 600 000 cases of bankruptcy were declared. In Australia, 81 % of the bankruptcy cases brought before the courts in 2005/2006 concerned individuals. In 2006, 106 629 cases of bankruptcy (either liquidation or proposals) were heard by Canadian courts.

- b) joint responsibility in credit provision, based on
 - i) acceptance by the applicant of the obligation to inform the credit provider truthfully about his/her situation and
 - ii) acceptance by the provider of the obligation to do everything within his/her power to compile an accurate assessment and give the applicant sound advice ⁽⁴⁴⁾;
- c) the possibility of cost-free credit transfers;
- d) the monitoring of advertising, marketing and commercial communications on consumer credit;
- e) 'credit scoring' parameters and a ban on entirely automated decisions;
- f) the guarantee of a basic banking service and that bank accounts will be universal and transferable and that accounts will be accessible via electronic means (debit cards);
- g) the definition of parameters for microcredit and other types of social credit and the promotion of 'alternative' financial institutions geared specifically to these sectors;
- h) identification and sanctioning of unfair commercial practices and of abusive clauses relating specifically to credit provision;
 - i) the right to withdraw from a contract;
 - j) delimitation of the requirement for collateral personal guarantees;
 - k) rules on commissions;
 - l) regulations governing credit brokers;
- m) strengthening the powers and supervisory measures available to the national authorities responsible for financial services in this area; and
- n) establishing parameters for defining what constitutes usury;
- o) adding a provision to the Consumer Credit Directive obliging banks to reply to complaints by a specified deadline.

In addition, in the long term, laws should be drawn up on the following aspects:

- a) a standard social insurance scheme;
- b) the guarantee of sustainable pensions schemes and their standard use in all Member States (possible definition of a '28th scheme');
- c) the definition of a system of single credit history files which fully respects personal data protection requirements and stipulates who can access the file and the purpose for which the information is intended (limited to the granting of credit).

⁽⁴⁴⁾ Good examples of this include Sections 79 to 81 of South Africa's National Credit Act No 34/2005.

6.3.2.2 At the same time, the Commission should encourage good practice in this field, promoting the adoption of European Codes of Conduct, in a system of self- or co-regulation, as part of a well-defined, effectively implemented coercive legal system.

6.3.2.3 The Commission should also, at its own initiative or in cooperation with the Member States, set up specific information programmes, educational measures focusing on the practical aspects of credit use and projects for providing support and advice in this area, making use of 'pilot project' instruments that have yielded such positive results in other areas ⁽⁴⁵⁾.

6.3.2.4 Lastly, the EESC suggests that a European Indebtedness Observatory be set up to work together with existing national bodies and others established in the Member States, to provide a forum for dialogue between all parties concerned, analyse developments in the phenomenon at European level and propose and provide back-up for the most appropriate prevention initiatives, subsequently assessing the impact thereof. The EESC here and now offers to house this observatory within its own institutional framework, at least until it becomes an independent body.

6.3.3 Dealing with debtors and recovery of assets

6.3.3.1 Given the diversity of systems set up at national level, which have varying origins, principles and methods ⁽⁴⁶⁾, the Commission's efforts should primarily focus not on attempts to secure harmonisation, but rather on defining a reference framework and a set of fundamental principles that should be guaranteed by all procedural law systems covering prosecution for unpaid debt or debt recovery from individuals, encouraging the adoption of these principles and enforcing recognition thereof.

6.3.3.2 The most important of these fundamental principles are:

- rapid solutions accessible to the parties concerned at little or no cost, which do not hinder access to credit or stigmatise debtors and their families;
- measures which take account of creditors' legitimate interests, but also of their responsibilities as regards household indebtedness;

- solutions favouring consensus and the conclusion of voluntary out-of-court payment agreements which make it easier for debtors to hold on, wherever possible, to assets essential to their family's wellbeing, such as the home;
- flexible measures enabling debtors to opt, in the most serious cases, to liquidate their attachable assets, with the forgiveness of unpaid debts taking due account of the situation of third parties who have stood guarantee for the debtors;
- specialist monitoring of debtors throughout the process of implementing post-bankruptcy payment plans, in order to prevent the same problems re-occurring and help debtors change their patterns of consumption and indebtedness, so that they can make a genuinely fresh start.

6.3.3.3 All of this work should, however, be opened up to involve the stakeholders and their representatives. It is suggested, therefore, that prior public consultation be held by means of the publication of a Green Paper defining the terms of the matter in hand, quantifying it at European level, analysing the different means and systems for preventing, monitoring and remedying situations of over-indebtedness and concluding with an outline for integrated action at Community level between the various Directorates-General concerned and also involving the authorities and civil society organisations in the various Member States and at Community level ⁽⁴⁷⁾.

7. Public hearing

7.1 On 25 July 2007, the EESC held a public hearing on the subject of this opinion, attended by a number of guest participants who are specialists in this field.

7.2 On the basis of the opinions expressed at a very well-attended session which produced a number of extremely useful papers, there was clearly considerable support for the aims of this opinion, which takes on board many of the suggestions made at the event.

Brussels, 25 October 2007.

The President
of the European Economic and Social Committee
Dimitris DIMITRIADIS

⁽⁴⁵⁾ There are, for example, cases of mediation and extrajudicial consumer dispute settlement projects which paved the way for the different networks currently in place in Europe; one of the most relevant of these to the matter in hand is 'Consumer DebtNet', established in 1994 and currently being redesigned under the name 'European Consumer Debt Net (ECDN)'.

⁽⁴⁶⁾ Moreover, some Member States, such as Portugal, still have no appropriate system for this purpose.

⁽⁴⁷⁾ In fact, the 2000 EESC information report referred to above concluded by recommending that the Commission 'make an initial move in this direction by immediately preparing a Green Paper on Household Over-indebtedness in Europe, incorporating available research into the issue, providing an up-to-date picture of legal arrangements and statistical data from the Member States and the applicant countries, working towards a single definition of over-indebtedness, and defining its preferred approach to achieve the objectives identified in the present information report'.