

Consumer Credit Directive: the Update

■ Ian Norman, 4th Jan 2010

Hot on the heels of the changes brought about by the Consumer Credit Act 2006, comes the anticipated European Consumer Credit Directive ('CCD'), which is to be implemented into UK law on 11 June 2010.

The UK Government is set to amend existing law in order to implement the CCD, which although wide reaching, will not affect all types of credit agreement currently regulated under existing law. In this 10 page guide, Ian Norman considers the scope and impact of this further wave of changes to greet the consumer credit industry:

■ The Scope

The CCD will not apply to a number of agreements that are currently regulated by the Consumer Credit Acts of 1974 and 2006 ('the current law'). These include:

- Lending to small businesses, partnerships and unincorporated bodies;
- Loans below £160;
- Loans above £60,260;
- Second charge mortgages;
- Hire purchase agreements;
- Credit with no interest or other charges and credit repayable within 3 months with no interest and only insignificant charges;
- Pawn broking; and
- Consumer hire agreements.

The result of the above is the risk that the different types of credit provided by lenders will be the subject of differing rules, depending upon whether or not they fall within the scope of the CCD. The government has recognised that this would be unhelpful and has indicated that lenders will have a choice either to comply with the CCD or the current law in respect of such types of credit (see below). However, it should be noted that lenders will not be permitted to offer some loans under the CCD and others under the

current law. Lenders will have to make a decision as to which route to follow, and then stick to it.

■ Exemptions

■ High Net Worth (HNW) Exemption – s.16A of the Consumer Credit Act 1974

The HNW exemption will face amendment, despite having only been brought into the current law in April 2008. The Government plans to amend it so that it will only be available for agreements that provide credit of more than £60,260.

■ Short-term loans

The exemption in respect of loans to be repaid within 12 months in no more than 4 installments will be modified. Under the amended legislation, credit repayable within 12 months by not more than 4 installments will only be exempt if it is provided without interest or any other charges. Further, running account credit agreements for credit repayable by one payment within 3 months and with insignificant charges will be exempt.

■ Low-cost credit and employee loans

Only loans made pursuant to statute will be exempt under the new regime. The interest rate must be less than that prevailing on the market, or at a rate which is not higher than that prevailing on the market where the other terms on which credit may be provided are more favourable to the borrower than those prevailing on the market. This replaces the current exemption for interest rates of no more than 1% above base rate.

The Government appears to be planning to implement the exemption in the CCD for loans made by employers to employees, as part of a secondary activity, free of interest or at interest rates lower than those prevailing on the market and which are not offered to the public generally. With reference to 'secondary activity,' it appears as if employees of financial institutions will still be able to benefit from low costs unregulated loans, as an employee is not a consumer for the purposes of the CCD. Therefore,

regardless of whether the lending to the employee is a primary or secondary activity, it will fall outside the scope of the CCD.

■ Pre-contractual Information

The Consumer Credit (Disclosure of Information) Regulations 2004 are facing an overhaul by virtue of the new Consumer Credit (Disclosure of Information) Regulations 2009. The 2004 regulations will continue to apply to:

1. Agreements secured on land;
2. Agreements for credit over £100,000; and
3. Agreements entered into “wholly or predominantly for the purposes of a business carried on, or intended to be carried on.”

In respect of agreements falling within 1-3 above (the exempt agreements), lenders will have the choice of either complying with the 2009 regulations, or the 2004 regulations.

The 2009 regulations provide that a creditor must “within good time¹” provide the borrower with pre-contractual information in the manner set out in the Standard European Consumer Credit Information (SECCI) form.

Lenders will have to update their pre-contractual documentation and systems to ensure compliance with the CCD. The pre-contractual information must be provided in exactly the same format as the SECCI in order to ensure compliance with the new requirements.

Lenders who lend exclusively under non-CCD products can benefit from complying with the current law relating to pre-contractual information and will not need to update their paperwork or systems. Those who offer products under both regimes may prefer to adopt a consistent approach and therefore adapt to the SECCI for all products in their portfolio.

■ Contractual Information

The format of credit agreements will have to be adapted to comply with the CCD. Exempt agreements listed at 1-3 above will still be governed by the Consumer Credit (Agreements) Regulations 1983; however, Lenders will have the choice of either complying with the 1983 regulations or the new Consumer Credit (Agreements) Regulations 2009 when eventuality brought into force.

¹ Defined in the 2009 regulations as being “at the earliest opportunity and without unreasonable delay”

The information, which will be required under the new 2009 regulations, will be similar to that already required under the 1983 regulations, subject to the following:

- Details of the borrower’s right to request an amortisation table, free of charge, in relation to fixed-term loans where repayments immediately reduce the capital balance outstanding;
- Where the repayments do not immediately reduce the capital balance outstanding, a statement showing the periods and conditions for the payment of interest and any associated charges; and
- Details of how the borrower can withdraw from the credit agreement.

In view of the above, changes will be required to loan documentation transacted once the new regulations come into force.

One interesting and noteworthy change, is that there is no prescribed format for the information to be included in agreements under the new regime. Instead, the obligation is upon lenders to specify the information in a clear and concise manner. The UK government has indicated that it will repeal the provisions of the current law, which go further than the CCD i.e. the rules which state that lenders must specify information in a particular order, without interspersing.

■ Advertising

New Consumer Credit (Advertisements) Regulations 2009 will be introduced and will replace the existing 2004 regulations of the same title. However, the new regulations will not apply to agreements to be secured on land, which will still be governed by the exiting 2004 regulations.

The new regulations introduce significant changes to the regulations in respect of advertising. They place an increased burden on lenders seeking new business through advertising media with the following key requirements, where any advertisement states an interest rate or any other figure relating to the cost of the credit to the borrower:

- the borrowing rate (fixed, variable or both);
- particulars of any charges included in the total charge for credit;
- the APR;
- the duration of the agreement;
- in the case of deferred payments for specific goods, services, land or other things, the cash price and details of any advance payment;
- the total amount payable by the borrower; and
- The amount of the instalments.

The APR included in the advertisement should be at or below that which the advertiser reasonably expects, on the date at which the advertisement is published, that credit would be provided in at least 51% of agreements entered into with borrowers as a result of the advertisement.

The above elements will form the “standard information” within what will be known as a “representative example.” Where the amount of credit is unknown and the advertisement relates to running account credit, the representative APR should be based on credit of £1200.

Clearly, these changes are fundamental and replace the “typical APR” required to be stated under the old regime. Lenders should ensure that they are up-to-date before seeking new business once these new regulations are implemented, which is scheduled for 11 June 2010.

▪ **Assignment of Rights**

Once the new law is implemented, a lender who assigns his rights to a loan to a third party will have to give notice of this assignment to the borrower, unless he agrees with the assignee that he will continue to deal with the borrower and therefore the arrangements for administering the credit to which the assignment relates remain unchanged.

This will mark a change in UK law for equitable assignments, although many lenders who sell portfolios of credit agreements (or their third party administrators) will continue to deal with borrowers and so will not be affected by this.

▪ **Credit Intermediaries**

New obligations will fall upon credit intermediaries, which will include those who carried out credit brokerage business under the old regime. Such “credit intermediaries” will be required to disclose in any advertising, or information provided to prospective borrowers, the extent of their powers (whether they can offer loans or simply forward application forms to lenders) and whether they act exclusively for one or more creditor, or as an independent.

In addition to the above, when conducting business, they will have to disclose to the borrower any fee payable for their services before the borrower is obliged to pay it. Any agreement to pay such a fee must be made between the borrower and the credit intermediary, in writing, before the credit agreement is entered into. They will also have to disclose the amount of any such fee to the lender so that it can be included in the lender’s calculation of the total charge for credit.

Any credit intermediary who fails to comply with the above will commit an offence under the Act.

▪ **Open End Agreements**

Regulated credit agreements with no fixed term will be cancellable by the borrower at any time, free of charge, by the giving no more than one month’s notice. A lender will be able to terminate such an agreement by the giving of not less than two month’s notice, in writing.

In order to avoid the need for numerous modifying agreements, the new provisions to be inserted into the 1974 Act will state that if a regulated open end agreement made before 11 June 2010 contains provision entitling the lender to terminate the agreement, any such provision shall be deemed to include a requirement for written notice of not less than two months to be given before termination takes place. This does not apply where termination is by reason of breach of the agreement.

Also, it is worth mentioning that subject to certain requirements, lenders will have the right to restrict the borrower’s right to draw upon credit under open end agreements.

▪ **Linked Agreements**

A new section 75A will be inserted into the 1974 Act in order to ensure that the UK’s European obligations are met. This new section will apply where the borrower does not have a claim against the creditor under section 75 itself, which will remain intact. This new section will not apply to agreements for credit of less than £160 or exceeding £60,260.

▪ **The Borrowing Rate**

The way in which lenders are required to notify borrowers of changes to the borrowing rate will be changed. Changes to the Consumer Credit (Notice of Variation of Agreements) Regulations 1977 will mean that notice of any variation will have to be given “without delay” rather than not less than 7 days before the variation takes effect.

With regard to changes in borrowing rate, particulars of the modified borrowing rate, details of the amount of repayments and where the number or frequency of the repayments is altered by the modification of the borrowing rate, details of any change in this regard. This will not apply to overdrafts.

It should be noted that when the borrowing rate changes as a result of a change in a reference rate (e.g. a base rate) then the parties may agree that the borrower may be given particulars regularly, in the form of statements, where the new reference rate is made available publicly and the information is also kept available at the lender’s premises.

■ Overdrafts and overrunning

Overdrafts are set to benefit from a 'light touch' form of regulation under the Directive, provided that they are repayable on demand or within 3 months.

PLEASE NOTE

This information is intended to provide a general overview and is not intended to provide legal advice.

■ Pre-contractual information

For new overdraft agreements meeting the above criteria, lenders will have to provide certain information to the borrower in good time and will have the option of using the format specified in the European Consumer Credit Information for Overdrafts, which is similar to the SECCI but specifically for overdrafts.

The pre-contractual information required for overdrafts should be given in good time, unless the borrower requests that the overdraft be made available with immediate effect, in which case only certain limited information need be given at the time of the request. The remainder of the information must be given to the borrower in good time afterwards, in order for the agreement to be properly executed.

■ Post-contractual information

For existing overdrafts meeting the above criteria, lenders will have to inform the borrower, at least annually, of the following:

1. The borrowing rate, the conditions governing the application of the borrowing rate and any index or reference rate applicable to the initial borrowing rate; and
2. The charges applicable and the conditions under which those charges may be changed.

Where the amount a borrower is overdrawn is significant and the account is overdrawn for a period exceeding one month, the lender must inform the borrower in writing of the account being overdrawn, the amount involved, the borrowing rate and any penalties, charges, or interest on arrears.

Lenders should now be considering the ways in which the above changes will affect their business systems and processes in time for the implementation of the changes, which is due to happen by no later than 10 June 2010.

For further information or advice in relation to the CCD, or the Consumer Credit Act and attendant Regulations, please contact:

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