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Consumer Protection in EU Residential Mortgage Markets: Common EU Rules on Mortgage Credit in the Mortgage Credit Directive

TATJANA JOSIPOVIĆ[1]

Abstract

For many years now, there has been an attempt in the European Union to create a common legal framework for mortgage credit contracts and cross-border activities in the mortgage financial sector. One of the greatest challenges has been the establishment of a corresponding level of consumer protection in EU residential mortgage markets. This issue has become particularly important at the time of financial crisis. Consumers are increasingly exposed to the risk of losing their homes because of failing to fulfil, in due time, their obligations arising from mortgage loans, and thus losing confidence in the EU financial sector. Therefore, the European Union has intensified its efforts to improve consumers' ability to inform themselves of the potential risks when entering into mortgage loans and mortgaging their real property. On 4 February 2014 the EU adopted the new rules on mortgage credits in the Mortgage Credit Directive. The main objective of the Directive is to increase the protection of consumers in EU mortgage markets from the risks of defaults and foreclosures. A higher level of protection must be ensured by consumers' increased information capacity related to mortgage credits, as well as by developing a responsible mortgage lending practice across the EU. The Mortgage Credit Directive is also aimed at contributing to the gradual establishment of a single internal market for mortgage credits. In this chapter, the author analyses previous and current attempts by the EU to establish a uniform

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market of mortgage loans, and assesses the possible impact of the Mortgage Credit Directive on the protection of consumers in the market of mortgage credits and on the development of cross-border activities in the mortgage financial sector. Special emphasis is placed on the possible impact of the new EU rules on mortgages on national protection measures aimed at consumer protection at the time of financial crisis. The transposition of the Mortgage Credit Directive will undoubtedly contribute to a higher level of consumer protection when consumers enter into home loan contracts. However, the question arises whether, because of different levels of harmonisation of some rules laid down in the Directive, its implementation will actually contribute to an increase in cross-border home loans. The possibility for Member States to opt for increased consumer protection in some aspects of credit agreements when implementing the Directive, or the existence of different options for the exercise of individual rights that they may use cannot bring about an integration of mortgage credit markets.

I. INTRODUCTION

THE EFFICIENT FUNCTIONING of the residential immovable property market is highly important for economic wealth and social progress, both at the level of individual Member States and at the level of the entire European Union. Only a well-developed residential immovable property market with properly balanced protection of the interests of all participants can contribute to economic and social welfare. The establishment of well-balanced protection of all participants is particularly sensitive in the residential mortgage credit market where it is very important to balance various rights and interests: economic interests and the functioning of financial institutions on the one hand, and the human rights and social and economic interests of debtors (consumers) on the other. The problems connected with the establishment of balanced protection of all these rights and interests have in the past few years mostly arisen from the global financial crisis. The most recent statistics of 2013 in the residential mortgage market have shown that because of the financial crisis, in some EU Member States, these markets are developing at a different pace. In some, a modest increase in residential lending has recently been observed, while in others the impact of the crisis on the residential mortgage market is still negative.[2] This is most probably only one of the reasons why, at this point, there is no integrated residential mortgage market at the European level.

There are currently 28 different frameworks for mortgages and 28 different legal frameworks for residential mortgage credits in the EU. Each of these national residential mortgage markets functions separately and

[2] See the data published in: EMF HYPOSTAT 2013, www.hypo.org/Content/Default.asp?PageID=524.

independently, and development is primarily affected by specific national economic, social and cultural circumstances, as well as by the particularities of national legislation that regulates residential mortgage credits, consumer protection and other areas. The national legislation of EU Member States differs extensively, not only in the regulation of mortgage and other security rights on immovables, but also in the regulation of mortgage credit agreements. There are also differences in the types of security rights on immovables (mortgage, hypothec, fiduciary transfer of ownership, retention of title, etc),[3] conditions for the establishment of security rights, the enforcement of security rights, the rights and obligations of mortgagors and mortgagees, the publicity of land registers, the flexibility of security rights (ie, dispositions with secured claims and security rights), and the connection between secured claims and security rights (accessory/non-accessory mortgage).[4]

Regarding mortgage credit agreements, there are many differences in national legislation when it comes to early repayment rules (conditions for early repayment, the compensation regime for creditors), the method and formula for the calculation of annual percentage rates, property valuation, the enforcement of mortgage credits, consumer protection rules, etc.[5] As a result, there are no developed primary and secondary pan-European mortgage credit markets. Cross-border activities in the mortgage financial sector in the EU internal market are in principle conducted by setting up branches or subsidiaries in the territory of another Member State. In the long run, this actually means that mortgage financial services are provided for under

[3] Conceptual differences in individual security rights on immovables mostly ensue from the fact that some are typical of common law systems (ie mortgage), and some of civil (continental) law systems (ie hypothec). The most important differences are reflected in the legal effects of the establishment of security rights on immovables (conveyance of the mortgagor's title to the mortgagee, the establishment of an unlimited real right in favour of the mortgagee, conditional/fiduciary transfer of ownership to the mortgagee). For more, see S van Erp, 'A secure start for the development of European property law' in *Sicherungsrechte an Immobilien in Europa*, ed M Hinteregger and T Borić (Vienna, Lit Verlag GmbH & Co KG, 2009) 5; M Hinnteregger, 'Die Immobiliensicherheit in Europa—eine rechtvergleichende Skizze' in *Sicherungsrechte an Immobilien in Europa*, ibid, 42; V Sagaert, 'Harmonization of Security Rights on Immoveables: An Ongoing Story' in *Towards a European Civil Code*, ed A Hartkamp, M Hesselink, E Hondius, C Mak and E du Perron (Kluwer Law International BV, 2011) 1046–48.

[4] See eg the results of the comparative research of the legal regulation of mortgage in Europe published in verband deutscher pfandbriefbanken, Round Table 'Flexibility, Security and Efficiency of Security Rights Over Immovable Property in Europe', Schaubilder ENGLISH (Stand Bd III, 3. Erweiterte Auflage, Berlin 2012—Übersetzung gem Bd 50 vdp-Schriftenreihe) at: www.pfandbrief.de/cms/_internet.nsf/tindex/de_de_rtall.htm.

[5] See eg the results of the comparative research published in the White Paper on the Integration of EU Mortgage Credit Markets, ANNEX 3 (2007): ec.europa.eu/internal_market/finservices-retail/home-loans/integration_en.htm#whitepaper. See MB Aalbers, 'The Globalisation and Europeanisation of Mortgage Markets' (2009) 33 *International Journal of Urban and Regional Research* 400.

the law of the host Member State.[6] Only exceptionally are cross-border mortgage credit agreements concluded.[7]

In such a disintegrated residential mortgage credit market, we may justifiably wonder how to achieve greater integration of the market at the EU level in order to contribute to cross-border activities in residential mortgage lending and efficient and better protection of individual rights and interests. For many years now, there has been an attempt in the EU to create a common legal framework for mortgage credit contracts and cross-border activities in the mortgage financial sector. One of the greatest challenges has been the establishment of a corresponding level of consumer protection in the EU residential mortgage markets. This issue has become particularly important at the time of financial crisis. Consumers are increasingly exposed to the risk of losing their homes because of failing to fulfil, in due time, their obligations arising from mortgage loans, and thus losing confidence in the EU financial sector.

It ensues from past activities in the EU market integration of the mortgage financial sector that discussions and actions connected with the integration of mortgage credit markets have mostly been directed at the provision of optimal levels of simplicity, flexibility, legal security, transparency, consumer protection, the protection of SMEs and creditors.[8] Two possible options to achieve these goals, and to create an internal market for mortgage loans, have thus emerged: the introduction of common rules on EU mortgages, ie, the introduction of a common pan-European security right on immovable

[6] Cross-border provision of financial services is thus based on the TFEU rules on the freedom of movement of capital (Arts 63–66 TFEU), freedom of movement of services (Arts 56–62 TFEU) and freedom of establishment (Arts 49–55 TFEU).

[7] In such cases, a special problem can be the application of separate rules on the applicable law for mortgage agreements and credit agreements. When a credit agreement is entered into in a Member State and the immovable property securing the repayment of the credit is located in another Member State, the law applicable to a mortgage agreement, or to a credit agreement, may be different. A mortgage agreement as a contract relating to the right *in rem* in immovable property is governed by the law of the country where the property is situated (Art 4(1)(c) Rome I Regulation). This rule applies even in the case where a consumer concludes a mortgage agreement with a financial institution (Art 6(4)(c) Rome I Regulation). On the other hand, the applicable law for credit agreements is determined under the rules of the Rome I Regulation on freedom of choice (Art 3) and on the applicable law in the absence of choice (Art 4), or, in the case of consumers' credit agreements, under the rules referred to in Art 6 of the Rome I Regulation. (See Ch König, 'The creation of an internal market for mortgage loans: A never ending story?' (2013) 2 *European Policy Analysis*). Every foreign investor who secures his loan with an immovable in another Member State must, therefore, acquaint himself with its national legal system in order to adjust (if this is even possible) the conditions of his loan and its security to a different legal framework from the one in his country. This is usually very time consuming and costly. In situations of a single or occasional cross-border provision of services, it is often also not commercially cost-effective. For more on consumer protection in the Rome I Regulation see Christophe Bisping, 'Consumer Protection and Overriding Mandatory Rules in the Rome I Regulation' in *European Consumer Protection*, ed J Devenny and M Kenny (Cambridge University Press, 2012) 239–56.

[8] For more, see under Sections II. and III.

property (Euromortgage/Eurohypothek) and/or the creation of common rules on mortgage credit agreements. Both of these approaches to integration call for answers to numerous questions concerning the choice of an optimal legal instrument for integration, the determination of personal and substantive areas of harmonisation, and the determination of the optimal level of cogent EU norms in the area of mortgage credit agreements. A crucial dilemma is whether to unify or merely to harmonise (adjust) the rules on mortgage and mortgage credit agreements; whether to carry out adjustment by minimum or maximum harmonisation, or whether to conduct full or targeted harmonisation. In terms of the personal and substantive area of harmonisation, a dilemma arises about whether harmonisation should encompass all mortgage credits or only consumer mortgage credits, cross-border and/or only domestic mortgage credits, all mortgage credits, or only residential (home) mortgage credits. There is a question, after all, about whether all aspects of mortgage credit agreements should be harmonised, or only some of them. There are still ongoing discussions on many of these questions. However, in the area of the protection of consumers in the mortgage credit market, the EU has already adopted some concrete measures.

In this chapter, the author analyses possible options for the integration of the EU internal mortgage credit market. In the first section of the chapter, some ideas, projects, possibilities and perspectives for the introduction of a common model of security rights at the European level (*Eurohypothek*) are presented. In the second section, an analysis is made of EU initiatives to integrate the mortgage credit markets resulting in the adoption of the Mortgage Credit Directive 2014/17/EU (MCD)[9] on 4 February 2014. This Directive sets out the current position of EU institutions on how, to what extent and in which segments it is necessary to integrate mortgage credit markets at the level of the EU and to establish common EU rules on mortgage credit agreements. The objectives of the Mortgage Credit Directive are analysed, as well as the level and scope of harmonisation. Finally, a possible transposition of the Mortgage Credit Directive for the protection of consumers in the mortgage credit market is assessed, and for the subsequent process and dynamics of EU market integration in the mortgage financial sector. The transposition of the Mortgage Credit Directive will undoubtedly contribute to a higher level of consumer protection when consumers enter into home loan contracts. However, the question arises whether, because of the different levels of harmonisation of some rules laid down in the Directive, its implementation will in fact contribute to an increase in cross-border home loans. The possibility for Member States to opt for increased consumer protection in some aspects of credit agreements when implementing

[9] Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directive 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 [2014] OJ L60/34.

the Directive, or for different options to exist whereby consumers may exercise individual consumer rights, cannot bring about an integration of mortgage credit markets.

II. 'EUROMORTGAGE/*EUROHYPOTHEK*' AS A MODEL FOR THE INTEGRATION OF THE MORTGAGE CREDIT MARKET

In the European Union, discussions on the introduction of a common pan-European security right on immovable property as collateral for securing loans started from as early as the mid-1960s. At different levels, academic, professional (within the framework of banking and notary public associations) and institutional (involving the competent bodies of the EU), various projects, research activities and discussions were organised and European legal documents were drafted, aiming to find an optimal model for a European system of securing claims by mortgages. Analyses, research activities and discussions on these issues resulted in different answers and proposals concerning ways to develop a common European mortgage credit market.[10] Despite the existing differences, all the initiatives were based on the same idea: an efficient common European mortgage credit market could best be established by the introduction of a new and special European model of securing loans by mortgage, the so-called *Eurohypothek* or Euromortgage. This would be a security right on immovables existing in parallel with 28 national legislative schemes regulating security rights on immovable property. The Euromortgage would be a security right on immovable property governed by separate rules uniformly applied in all Member States. These rules on the Euromortgage and its legal nature, acquisition, disposition, protection, settlement and on the legal relations between a mortgagor and a mortgagee would apply regardless of where the encumbered immovable property was located. This specific European model of a security right on immovables would have to be designed in such a way as to represent a flexible instrument of security for both creditors and debtors, whereby all parties ought to be provided with the corresponding legal protection both in their mutual relations and in their relations with third persons. An appropriate balance in the realisation of their interests and possible conflicts should also be ensured.

The model should not provide an efficient security right only for creditors. The Euromortgage should not only be an instrument for securing claims but also an instrument by which the value of immovables is efficiently mobilised in the common European market and in legal transactions other than

[10] For more, see Sagaert (n 3 above) 1054–62; van Erp (n 3 above), studies and reports on the integration of EU mortgage markets by expert groups established by the European Commission at: http://ec.europa.eu/internal_market/finservices-retail/credit/mortgage/index_en.htm#maincontentSec3.

credit contracts comprising various financial transactions. Therefore, all the proposals for the introduction of the Euromortgage, although they differ with regard to the regulation of individual aspects of this legal institution, in principle define its basic features in the same way. The Euromortgage should cumulatively fulfil the following conditions: it should be (a) a non-accessory right whose establishment and existence should not be conditioned by the existence of a valid claim secured by it;[11] (b) a registered right acquired by an entry in the corresponding register, where such an entry fulfils the requirement of publicity towards any third persons and offers the possibility of its being used against any third persons; (c) a right incorporated in securities.

However, there are differences among individual projects dealing with the introduction of the Euromortgage in terms of the extent to which and how some of the mentioned features should be manifested in the regulation of the Euromortgage. These differences largely arise from the fact that, in some projects, various models of lien, already existing in individual legal orders, have been used for the regulation of the Euromortgage. In the current practice and because of their features, they have proven to be successful instruments for securing claims. The two basic models used in the proposals for the regulation of the Euromortgage have been the German *Grundschuld* and the Swiss *Schuldbrief*. Both these instruments are characterised by the fact that, in a particular way but with a different theoretical explanation, they unify all three features highlighted above as necessary for the efficiency of the Euromortgage in the European market of mortgage credits and for its flexibility in the financial market.

One of the first initiatives for the introduction of a common pan-European mortgage was the 'Segré Report' of 1966.[12] The European Commission organised a task force led by Professor Claudio Segré which developed an extensive report entitled 'Development of the European Capital Market' (the Segré Report) dealing with the problems ensuing from the liberalisation of the circulation of capital and the implications of

[11] The accessoriness or non-accessoriness of the security right on immovables depends on the legal nature of the relationship/connection between the secured claim and the security right. Accessory security rights are characterised by a strong legal connection between the security right and the security claim. The emergence, existence, termination and the exercise of a security right depend on the existence of a valid and enforceable secured claim. When it comes to non-accessory security rights, a security right exists regardless of a secured claim. A non-accessory security right may be disposed of independently of a secured claim. A person other than the holder of a secured claim may be the holder of a non-accessory security right. Therefore, non-accessory security rights are considered to be more flexible in legal transactions. For more on the types or effects of accessoriness, see OM Stöcker and R Stürner, *Flexibility, Security and Efficiency of Security Rights over Real Property in Europe vol III* (Berlin, Verband deutcher Pfandbriefbanken, 2010) 44.

[12] *The Development of a European Capital Market*, Report of a Group of experts appointed by the EEC Commission, Brussels, November, 1966 (Segré Report): http://ec.europa.eu/economy_finance/emu_history/documentation/chapter1/19661130en382develeurocapitm_a.pdf.

the establishment of an integrated capital market.[13] Among other things, harmonisation of the national legislation of the Member States on security rights on immovables was proposed. The German *Briefgrundschuld* was recommended, ie non-accessory liens on immovables incorporated in securities (*Grundschuldbrief*).[14] The task force was of the opinion that such a model for the real property security of claims could instigate the integration of the capital market among the Members States. It could, at the same time, play a particularly important role when it comes to housing loans because it is a cheaper and more flexible instrument of security than an accessory mortgage.[15,16] The Segré Report was followed by the proposal of the Union of Latin Notaries where, for the first time, the name Euromortgage was given to a single European model of security rights on immovables.[17] In its Report of 22 May 1987,[18] the Union of Latin Notaries officially proposed the introduction of a single real property security on immovables—the Euromortgage. According to the Report, it was meant to exist in parallel with other security rights on immovable property already existing in some Member States and it would be regulated on the model of the Swiss *Schuldbrief*.[19] The Euromortgage would be defined as a non-accessory security right on immovable property[20] whose application would eliminate/remove the barriers to the cross-border establishment of security rights on immovables. It was emphasised that the Euromortgage should be an optional security right provided for in European law which would exist along with the national security rights on immovables. It was believed that such a 'European' security right would remove legal, economic and

[13] For more, see O Stöcker, *Die Eurohypothek* (Berlin, Duncker & Humblot, 1992) 216, 217.

[14] See Stöcker (n 13 above) 216, 217; S Kircher, *Grundpfandrechte in Europa* (Berlin, Duncker und Humblot, 2004) 442.

[15] See Stöcker (n 13 above) 217.

[16] The accessoriness of security rights means the following: a security right only exists if a secured claim also exists (accessoriness of origin); the scope of a security right is determined by the amount of the secured claim (accessoriness of scope); the holder of the security claim (creditor) is always the holder of the security right (accessoriness of competency); a security right terminates with the extinguishment of the secured claim (accessoriness of extinguishment); a security right can be enforced only if the secured claim is capable of enforcement (accessoriness of enforcement). These types of accessoriness are taken over from Stöcker, Stürner (n 11 above) 44.

[17] Since then, *Eurohypothec* started to be used as a common name for all other proposals for a universal European real property security instrument on immovables and even in EU documents where the possibility of its introduction was considered.

[18] A shortened version of the Report with the proposals was published in the German language in HG Wehrens, 'Der schweizer Schuldbrief und die deutsche Briefgrundschuld—Ein rechtvergleich als Basis für eine zukünftige Eurohypothek' (1988) 7 *Őesterreichische Notaritars Zeitung* 181–91; HG Wehrens, 'Überlegungen zu einer Eurohypothek' (1992) 14 *Wertpapier-Mitteilungen WM Zeitschrift für Wirtschafts- und Bankrecht* 557–96.

[19] The regulation of *Eurohypothec* on the model of the Swiss *Schuldbrief* is explained by the fact that the Swiss *Grundschuld* as a non-accessory security right is even more flexible as a security instrument than the German *Grundschuld*. See Stöcker (n 13 above) 229; Wehrens, 'Überlegungen zu einer Eurohypothek' (n 18 above) 560.

[20] See Wehrens, 'Überlegungen zu einer Eurohypothek' (n 18 above) 560; HG Wehrens, 'Das Grundbuch als Finanzierungsinstrument' (1993) *Notariatszeitung* 69, 70.

practical deficiencies of strictly accessory security rights in the national legal orders of Member States.[21]

A more concrete determination of the Euromortgage was laid down in the 'Basic Guidelines for the Eurohypothec' of 2005.[22] These Guidelines represent a kind of 'model law' where all important aspects of the legal regulation of the Euromortgage were provided for. They constitute the most concrete and developed model of the Euromortgage[23] that describes its basic features and the principles on which it is based, as well as its establishment, publication, disposition, termination, the protection of trust and the right of settlement against the value of immovables, and its position in bankruptcy proceedings and its implementation in the national legal orders of Member States. Both the German and Swiss models had an impact on the proposed model of the Euromortgage, so that individual solutions were the result of the unification of some elements of the German *Grundschuld* and the Swiss *Schuldbrief* as the best practices in credit transactions. The Euromortgage is again defined as a non-accessory security right entitling its holder to the settlement of a specified pecuniary amount against the value of the immovable (Article 2.1). In the Guidelines, non-accessoriness is emphasised as the most important feature of the Euromortgage (Articles 12, 2.1). It is expressly laid down that the establishment, transfer and existence of the Euromortgage and the exercise of the right to settlement do not depend on the existence of a secured claim (Article 3.4). However, the separation of the Euromortgage from the secured claim is bridged with a so-called security agreement establishing a contractual connection between the secured claim and the security right, and a specific fiduciary relation between the owner of the immovable and the creditor.[24] In addition, according to the

[21] See Wehrens, 'Der schweizer Schuldbrief' (n 18 above) 181; Wehrens, 'Überlegungen zu einer Eurohypothek' (n 18 above) 559; Kircher (n 14 above) 483; O Stöcker, 'The Eurohypothek' in *The Future of European Property Law*, ed S van Erp, A Salomons, B Akkermans (Munich, Sellier European Law Publishers, 2012) 75.

[22] See Agnieszka Drewicz-Tułodziecka (ed), *Basic Guidelines for a Eurohypothec: Outcome of the Eurohypothec Workshop, November 2004/April 2005* (Warsaw, Mortgage Credit Foundation, 2005). The Guidelines are developed in cooperation with experts gathered in a research group called 'The Eurohypothec: A Common Mortgage for Europe', members of the subgroup 'Collateral' working within the 'Forum Group on Mortgage Credit' established by the European Commission, a representative of the European Land Information Service/EULIS and experts from various Member States gathered around the project 'Real Property Law and Procedure in the European Union' at the European University Institute in Florence.

[23] G Watt, 'The Eurohypothec and the English Mortgage' (2006) 2 *Maastricht Journal of European and Comparative Law* 175; Stöcker, 'The Eurohypothek' (n 21 above) 73, 74; S Nasarre-Aznar, 'The need for the integration of the mortgage market' in *Europe, The Future of European Property Law*, ed S van Erp, A Salomons and B Akkermans (Munich, Sellier European Law Publishers, 2012) 96–98.

[24] The security agreement stipulates under what conditions the holder of the Eurohypothec may keep and enforce the Eurohypothec (Arts 2.2, 4.1, 4.2). If the creditor exercises his rights under the Eurohypothec contrary to this agreement, the owner of the immovable is entitled to the compensation of damage (Art 4.3).

Guidelines, the Euromortgage is a registered security right (Article 3.2) and it can also be designated as a certified (letter) right (Article 3.3).

Despite these concrete initiatives for the legal regulation of the Euromortgage, so far no concrete measures have been adopted at the EU level for the introduction of the Euromortgage as a European optional security right. There are several reasons for this. One is undoubtedly the existence of limited EU competences for the introduction of the Euromortgage. There is no doubt that the mortgage credit market is part of the financial market and that the TFEU provisions on free movement of capital apply accordingly.[25] However, it is questionable whether, on the basis of EU competences for the adoption of approximation measures for the establishment and functioning of the internal market (Article 114 TFEU) and according to the principles of subsidiarity and proportionality (Article 5 TEU), the EU is really competent for the harmonisation of security rights on immovable property. It is also questionable whether all the prerequisites referred to in Article 352 of the TFEU could have been fulfilled so that the EU could possibly provide for the Euromortgage as an optional instrument which would exist as the 29th regime in parallel with 28 national legal regimes regulating security rights on immovables.[26] The reactions of Member States, financial institutions, associations of consumers and others regarding the need and justification for the Euromortgage have also been different and mostly very restrained. The European Commission incorporated the issues of justification of the Euromortgage in the 'Green Paper—Mortgage Credit in the EU'[27] of 2005. In discussion on this Green Paper—Mortgage Credit in the EU,[28] only a small number of those involved supported the idea of the introduction of the Euromortgage as a separate parallel security right on immovables (21 per cent of financial institutions, 31 per cent of Member States and 16 per cent of other participants). Those who supported the idea of

[25] See eg Case C-222/97 *Trummer v Mayer* [1999] ECR I-1661.

[26] Art 345 TFEU is very important for the harmonisation of security rights on immovables as a segment of property law. It states that 'The Treaties shall in no way prejudice the rules in Member States governing the system of property ownership'. In literature, viewpoints can be found that this provision does not exclude the whole of property law from the impact of European law. It is also emphasised that Art 352 TFEU may be a suitable legal basis for future optional instruments on EU property law. See E Ramaekers, *European Union Property Law* (Cambridge, Intersentia, 2013) 140, 220–23.

[27] Green Paper on Mortgage Credit in the EU (COM(2005) 0327) of 19 July 2005, final.

[28] In the Green Paper on Mortgage Credit in the EU, the Commission highlighted the question of regulation of security rights to secure loans as one of the key issues for the integration of the mortgage credit market. It referred to the recommendations for the introduction of the Eurohypothec (eg Basic Guidelines for the Eurohypothec) as a special optional non-accessory security right to be applied in the whole EU. It is characterised by increased flexibility and it would exist as a separate security right in parallel with the national regulations for mortgages. However, being aware of the complexity of the issue, particularly because it overlaps with many other legal areas such as substantive law and the law of obligations, the EC initiated consultations on the necessity and appropriateness of introducing the Eurohypothec.

introducing the Euromortgage believed that its flexibility could increase competitiveness, reduce interest and create better conditions for consumer credits. On the necessity to introduce the Euromortgage, participants in the discussion emphasised the need for further examination of the model, particularly with regard to its impact both on national legal regulations and on other legal areas (bankruptcy law, enforcement law, registration of immovables and others) and on the benefit for the protection of consumers. When it comes to the most important problem connected with the Euromortgage—its non-accessoriness—positions were also divided. While some were opposed to the abandonment of accessoriness to protect debtors, others advocated a more detailed elaboration of the idea of non-accessoriness. There were also those who, by referring to the positive experience in their national legislation, supported the idea of non-accessoriness of the Euromortgage.[29] Such reservations regarding the introduction of the Euromortgage, as well as increased problems in financing mortgage credits resulting from the financial crisis, contributed even more to the subsequent minimising of the Euromortgage as a model for the integration of mortgage credit markets.[30] Thus, the White Paper on the 'Integration of EU Mortgage Credit Markets' of 2007[31] no longer dealt with the problems of the introduction of the Euromortgage.[32] It only focused on defining measures to protect consumers in mortgage credit markets at the time of global financial crisis. For all these reasons, the question of introducing the Euromortgage as a model for the integration of mortgage credit markets remained open and was shifted to become only a subject of academic discussion.

III. COMMON EU RULES ON MORTGAGE CREDIT—A NEW APPROACH TO THE INTEGRATION OF MORTGAGE CREDIT MARKETS

EU initiatives in the area of mortgage credits have been mostly directed towards the protection of consumers in mortgage credit markets. Although it is clear from all EU initiatives aimed at the integration of mortgage credit markets that they are directed at creating a functional internal market for mortgage credits, facilitating their funding and increasing product

[29] For more, see 'Feedback on the Consultation on the Green Paper on Mortgage Credit 2006', 23 May 2006 MARKT/H3JR D(2006): http://ec.europa.eu/internal_market/finservices-retail/archive/mortgage_en.htm; AJM Steven, 'Accessoriness and Security over Land' (2009) 13 *Edinburgh Law Review* 421.

[30] See S van Erp, B Akkermans, 'European Union Property Law European Union Private Law, ed Ch Twigg-Flesner (Cambridge, Cambridge University Press, 2010) 181.

[31] White Paper on the Integration of EU Mortgage Credit Markets, 18 December 2007 [SEC/2007) 1683, SEC(2007) 1684] (COM/2007/0807 final). For more see S Nasarre-Aznar (n 23 above) 90, 91.

[32] The *Eurohypothec* is mentioned only in one of the annexes (Annex Three 'Impact Assessment of Specific Issues') as one of the models which could facilitate the cross-border transfer of mortgage loan portfolios (169).

diversity, the most significant emphasis is placed on improving consumer confidence and facilitating mobility to establish a single mortgage credits market. This was already obvious in the Commission Recommendation on pre-contractual information to be given to consumers by lenders offering home loans (2001),[33] resulting in the European agreement on a voluntary code on pre-contractual information for home loans.[34] Ever since 2003, the Commission has intensified its research on the level of integration of mortgage credit markets and the obstacles to their further integration which have blocked their development in order to determine the possible advantages of further integrating mortgage credit markets within the European financial market. Three different expert groups were organised and a number of studies developed dealing with the problems of mortgage credit markets[35] This resulted in the issuance of the Green Paper 'Mortgage Credit in the EU' (2005) in which the Commission presented its positions regarding possible interventions in the European mortgage credit markets. The European Parliament adopted its Resolution on Mortgage Credits in the EU (2006)[36] and subsequently the Commission published its White Paper on the Integration of EU Mortgage Credit Markets (2007). It ensues from all these documents issued by the Commission that the crucial question in the European mortgage credit markets is the protection of consumers. It is precisely the protection of consumers and their trust in mortgage credit markets which can be the main integrative element for the establishment of a single mortgage credit market. Therefore, the following issues were highlighted in the White Paper as the most important: improving the quality and comparability of information; promoting responsible lending and borrowing; rules on early repayment; the development of valuation standards; the transparency and reliability of land registers; and improving the efficiency of foreclosure procedures.[37] The Euromortgage is no longer referred to as a possible solution for integration. In short, the European institutions, when it comes to the further integration of mortgage credit markets, aim at the creation of common rules on mortgage credit agreements to ensure the greater protection of consumers founded on the principles of responsible borrowing and responsible lending as key factors of intensified cross-border

[33] Commission Recommendation of 1 March 2001 on pre-contractual information to be given to consumer by lenders offering home loans [2001] OJ L69/25.

[34] Agreement on the Code of Conduct and Register of Institutions adhering to the European Code are published at: http://ec.auropa.eu/internal_market/finservices-retail/home-loans/code_en.htm. For more on the implementation of the Code see HJ Dübel and M Rothemund, 'A New Mortgage Credit Regime for Europe—Setting the Rights Priorities' (2011) *Center for European Policy Studies/European Credit Research Institute*, EPS Special Report (www.ceps.eu/book/new-mortgage-credit-regime-europe-setting-right-priorities) 37–41.

[35] See expert group studies and reports on the integration of EU mortgage markets at: http://ec.europa.eu/internal_market/finservices-retail/archive/mortgage_en.htm.

[36] 2006/2012(INI): www.europarl.europa.eu.

[37] See White Paper on the Integration of EU Mortgage Credit Markets (n 31 above).

activities in the mortgage financial sector. This concept was adopted in the Mortgage Credit Directive of 4 February 2014, by which consumer protection at the European level is ensured when entering into residential mortgage credit agreements.

A. The Mortgage Credit Directive—Harmonisation of Consumer Mortgage Residential Credit Agreements

The Mortgage Credit Directive (MCD)[38] is the first adopted measure of the European Union which specifically provides for particular aspects of mortgage credit agreements.[39,40] The Directive is the result of several years of discussions on the 'Proposal for a Directive on credit agreements relating to residential property' of 2011.[41] It entered into force on 20 March 2014 and the Member States are bound to transpose it in their national legislation before 21 March 2016. The final adoption of the Mortgage Credit Directive was largely supported by the fact that 'the financial crisis had shown that irresponsible behaviour by market participants could undermine the foundations of the financial system, leading to a lack of confidence among all parties, in particular consumers, and potentially severe social and economic consequences'.[42] The existing problems that consumers had with loan credit agreements resulted in the final text of the MCD differing significantly from the Commission's first 'Proposal for a Directive on the freedom of establishment and the free supply of services in the field of mortgage credit' of 1985[43] and thus also from the Commission's 'Proposal for a Directive on credit agreements relating to residential property' of 2011.[44] In its proposal for the Directive of 1985, the Commission proposed to regulate only the issues connected with the exercise of the right to establishment and the right to provide services. In the proposal for the Directive of 2011, the emphasis was put on the protection of consumers in the cases of credit agreements relating to residential immovable property and certain aspects

[38] See n 9 above.

[39] This Directive was adopted on the basis of Art 114 TFEU which constitutes the basis for the harmonisation of consumer protection in Member States in the context of the completion of the internal market (Art 169(2)(a) TFEU).

[40] For more on previous attempts of the Commission to regulate EU mortgage credit markets see Ch König (n 7 above) 3, 4.

[41] The proposal for a Directive of the European Parliament and of the Council on credit agreements relating to residential property (text with EEA relevance), COM(2011) 0142 final—COD(2011) 0062.

[42] The quotation taken from Recital (3) of the Preamble to the Mortgage Credit Directive.

[43] Proposal for a Directive on the freedom of establishment and the free supply of services in the field of mortgage credit, Brussels, 7.2.1985, COM(84) 730 final (http://aei.pitt.edu/8826).

[44] Proposal for a Directive of the European Parliament and of the Council on credit agreements relating to residential property, Brussels, 31.3.2011, COM(2011) 142 final (http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52011PC0142).

of the prudential and supervisory requirements for credit intermediaries and creditors. In the proposal of the Directive of 2011, the emphasis was placed on consumer protection regarding pre-contractual information, the calculation of the annual percentage rate of charge, and early repayment.[45] However, in comparison with the proposed text, the final text of the MCD was much more extensive and detailed in the regulation of individual consumer rights. In the course of the discussion in the European Parliament, almost every provision in the proposal was amended and expanded[46] and special emphasis was placed precisely on the need to protect consumers from over-indebtedness with home loans and on the establishment of a system to promote sustainable lending and borrowing.[47] This is why numerous provisions on the financial education of consumers, on the protection of consumers from tying and bundling practices, and on a standardised information sheet for pre-contractual information, foreign currency loans, arrears and foreclosures and the like were added. In addition, many provisions in the proposal were amended to ensure greater consumer protection (eg early repayment, general information, adequate explanations, etc).

The MCD was adopted on the basis of Article 114 TFEU providing for the procedure of launching measures for the approximation of laws important for the establishment and functioning of the internal market. The reason for choosing Article 114 TFEU as the basis for the MCD was actually the only possible solution, because on the basis of that Article, the EU was authorised to adopt measures by which, in the context of the completion of the internal market, the economic interests of consumers were ensured (Article 169(2)(a) TFEU). The goals of the harmonisation to be achieved on the basis of Article 114 TFEU (the establishment and the functioning of the internal market) also determined the areas of harmonisation in the MCD. Therefore, the MCD harmonises only particular aspects of credit agreements relating to residential immovable property. For example, specific aspects of security rights on residential immovable property are not the subjects of harmonisation, although they may be of great importance for consumer protection. Likewise, specific aspects of consumer protection in foreclosure proceedings which, in cases of delayed payment, lead to the repossession of residential immovables are not the subjects of harmonisation, although they are one of the most frequent problems concerning consumer protection and home loans, particularly in the Member States affected by the financial crisis.

[45] See Arts 9, 12, 18 of the Proposal/2011.

[46] See the Amendments adopted by the European Parliament on 10 September 2013 on the proposal for a directive of the European Parliament and of the Council on credit agreements relating to residential property (COM(2011) 0142—C7-0085/2011—COD(2011) 0062): www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2013-0341&language=EN&ring=A7-2012-0202.

[47] See, eg p 3, 6 MCD – Text adopted by European Parliament (n 42 above).

i. The Main Objectives of the Directive

The main objectives of the Directive can be summarised as follows: (a) establishment of a high level of consumer protection; (b) prevention of irresponsible lending and borrowing, of unaffordable loans, and of defaults and foreclosures; (c) establishment of a high level of professionalism among creditors and credit intermediaries; (d) introduction of a passport regime for credit intermediaries; (e) establishment of an efficient and competitive single market for the benefit of consumers, creditors and credit intermediaries; and (f) promotion of financial stability on the internal market. In this respect, the Directive is a specific complement to the Consumer Credit Directive (CCD),[48] by which the laws, regulations and administrative provisions of the Member States covering consumer credit have been harmonised. Both directives supplement each other, widening the framework for consumer protection on the EU financial market and establishing a harmonised protective mechanism for various types of consumer credit agreements.[49,50] The Consumer Credit Directive generally applies to credit agreements (Article 2(1) CCD).[51] Due to the fact that the CCD does not apply to credit agreements secured by mortgage (Article 2(2)(a) CCD), the aim of the MCD is precisely the harmonisation of consumer mortgage residential credit agreements at the level of the European Union. For the most part, the MCD provides for the harmonisation of the same aspects of consumer credit agreements following the basic structure of the CCD, but taking into consideration particular characteristics of residential credit agreements and the very specific consumer protection needs of such agreements.

In order to meet these objectives, the scope of application of the MCD is determined in such a way that its application also encompasses so-called

[48] Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC [2008] OJ L133/66–92.

[49] Cf points 19, 20 of the Preamble to the Directive.

[50] In order to ensure harmonised protection of consumers in taking consumer loans, residential mortgage credits and home loans, there are various links (in individual articles of the Mortgage Credit Directive) between the CCD and MCD. Eg, in some of its articles, the MCD refers to the appropriate application of the CCD. Thus, the MCD, in Art 4 which outlines some definitions for the purpose of this Directive, only refers to the definitions given in the CCD, such as the definitions of 'consumer', 'total amount of credit', 'total amount payable by the consumer', 'borrowing rate', 'durable medium' (Art 4, points (1), (12), (14), (16), (18) MCD). On the other hand, the MCD in some cases leaves an option to Member States not to apply some provisions of the MCD to some credit agreements but only under the condition that they apply the provisions of the CCD (Art 3(3)(a), (e) MCD).

[51] The exceptions from the scope of application of the CCD are expressly laid down in Art 2(2) CCD. However, the MCD has expressly broadened the scope of application of the CCD regardless of these exceptions. Art 46 MCD expressly supplements the CCD by widening the scope of application also to unsecured credit agreements whose purpose is the renovation of residential movable property involving a total amount of credit exceeding €75,000.

'home loans', ie agreements relating to residential immovable property regardless of whether they are secured by a real security right on immovable property. The scope of application of the MCD covers, on the one hand, consumer credit agreements[52] secured by a real security right on residential immovable property, ie agreements secured by mortgage or another comparable security commonly used in a Member State, or by a right related to residential immovable property (Article 3(1)(a)). On the other hand, the Directive applies to credit agreements whose purpose is to acquire or retain property rights in land or in an existing or projected building (Article 3(1)(b)) and regardless of the fact that they are not protected by security on immovable property.[53] The scope of application encompasses only consumer[54] residential property agreements, irrespective of whether cross-border or domestic credit agreements are at issue. The Directive does not distinguish in any way the legal regulation of credit in immovable property agreements protected by security depending on whether the charged property is located in the state where the consumer resides or in another state.

Regarding consumer protection in credit agreements, it is irrelevant whether a mortgage agreement is made as a cross-border or a domestic agreement. For the Directive to apply it is decisive that a credit agreement relates solely and predominantly to residential immovable property, for such property is charged by a real security right either because the purpose of the credit agreement is the acquisition or retention of a property right in land or in an existing or projected building.[55] Other consumer credit agreements that relate to immovable property without any residential purpose are not covered by the Directive.[56] It is obvious that the main aim of the Directive is to establish common standards of consumer protection for credit agreements most frequently taken by consumers to ensure their elementary existential need for acquiring a home and satisfying their housing needs.

[52] For the purposes of the Directive, 'credit agreement' means an agreement whereby a creditor grants or promises to grant, to a consumer, a credit falling within the scope of the Directive (Art 3) in the form of a deferred payment, loan or other similar financial accommodation (Art 4(3) MCD).

[53] Credit agreements excluded from the scope of application of the Directive are expressly specified in Art 4(2) MCD.

[54] For the purposes of the Directive, 'consumer' is defined as in Art 3(a) CCD (Art 4(1) MCD). According to the MCD, 'consumer' is considered to be a natural person who, in transactions covered by the Directive, is acting for the purposes which are outside his trade, business or profession. 'Creditor' means a natural or legal person who grants or promises to grant credit falling within the scope of the Directive (Art 3) in the course of his trade, business or profession (Art 4(2) MCD).

[55] Cf Recital 13 of the Preamble to the Directive.

[56] The Member States may, however, extend the scope of application of the Directive also to credit agreements related to other forms of immovable property (recital 13 of the Preamble).

In order to establish a common framework of consumer protection, various levels of harmonisation of individual aspects of credit agreements relating to residential immovable property are envisaged, from the minimum to the targeted maximum, or to optional harmonisation. In principle, the adjustment of individual aspects of credit agreements regulated in the Directive is based on minimum harmonisation (Article 2(1) MCD). Therefore, the Member States may keep or transpose into their national legislation more stringent provisions in order to protect consumers. Maximum harmonisation is envisaged only for two aspects of credit agreements (so-called targeted maximum harmonisation) with regard to standard pre-contractual information (Articles 2(2), 14(4), Annex II) and to the standard for the calculation of the annual percentage rate of charge (Articles 2(2), 17(1) (5), (7), (8), Annex I). As for these rules, the Member States may neither keep nor introduce any rules different from those prescribed in the Directive, but are bound to establish the level of protection laid down in the Directive. Indeed, many provisions of the Directive leave the possibility for the Member States to use the option of not applying some articles on specified consumer mortgage credit agreements to allow, or provide, some specific practice or obligations for the parties to the agreement (so-called optional harmonisation).[57] At the same time, for all the provisions of the Directive, its imperative nature is expressly prescribed (Article 41). In order to ensure the optimum protection of consumers, the provisions on consumer protection incorporated in the national law by the transposition of this Directive must be compulsory (*ius cogens*). In their credit agreements, consumers may not waive the rights conferred on them (Article 41(a) MCD), and the parties, by entering into other types of credit agreements, may not avoid the application of the provisions implementing the Directive (Article 41(b) MCD).

The measures whose implementation in the national legislation should lead to an efficient and competitive single market for consumer mortgage residential credit agreements are different in their content. The Directive contains a series of measures providing for requirements for the establishment and supervision of credit intermediaries and appointed representatives.[58] The aim of their implementation is to introduce a so-called passport regime for credit intermediaries to ensure a high level of professionalism when making cross-border credit agreements and a simpler and safer cross-border provision of financial services (Articles 7–9, 22, 29–34). Most measures relate to the harmonisation of the national rules on credit agreements, particularly concerning creditors' pre-contractual obligations, some contractual elements, the rights of consumers when paying their credit commitments, and

[57] Compare, eg Arts 3(3); 7(5); 11(1); 12(2), (3), (4); 14(6); 16(2); 22(4), (5); 23(2), (5); 25(2), (3), (5); 27(2); 28(2), (3).
[58] Cf Arts 29–35 MCD.

the like. The goal of these measures is to prevent irresponsible lending and borrowing and defaults and foreclosures detrimental to consumers. Some of these measures must be implemented from as early as the pre-contractual phase, ie before entering into credit agreements, and some are implemented for the duration of credit agreements in order to make it easier for consumers to meet their obligations in a timely and proper manner. These will be considered in turn.

ii. Measures for the Prevention of Irresponsible Lending and Borrowing

According to the MCD, consumer protection in the pre-contractual phase is based on various measures, the common aim of which is to prevent irresponsible lending and borrowing, ie to prevent consumers from assuming unaffordable credit obligations which at the end of the day may lead to residential immovable property foreclosures. All these measures must ensure, both for consumers and for creditors, the making of informed and responsible decisions on whether to conclude a credit agreement, who to conclude it with and under what conditions. Such informed consumer decisions regarding the making of credit agreements are facilitated by measures which provide clearer and general information and which standardise the method of calculating the annual percentage of charge (APRC). Measures important for a creditor's decision on whether to enter into a credit agreement are those that will ensure an objective and regular assessment of the creditworthiness of the consumer in order to establish, in the pre-contractual phase, the consumer's real capacity to regularly meet his or her credit commitments.

iii. Clearer and General Information for Consumers

Clearer and better information for consumers in the pre-contractual phase is provided for in the Directive through various measures, from binding the Member States to promote measures for the financial education of consumers (Article 6 MCD), defining the principles for the conducting of business of creditors, credit intermediaries and appointed representatives (Articles 7, 8, 9 MCD),[59] to the obligation of providing information to consumers in various phases of the conclusion of the credit agreement (Articles 10–16 MCD). The Directive expressly lays down the rules on creditors' obligations in terms of standard information in advertising, general information

[59] The principles for conducting business must include the obligation to act honestly, fairly, transparently and professionally, to organise sound and effective risk management, to act in the consumer's best interest, to provide information free of charge to consumers, to have an appropriate level of knowledge and competence, the obligation for advertising to be fair, clear and not misleading, and the prohibition of tying practices. See Ch König (n 7 above) 4.

about credit agreements, information concerning intermediaries and representatives, and the obligations of providing adequate explanations and advice to consumers.[60]

When the pre-contractual obligations of providing information are at issue, a central place in the Directive is given to the creditor's obligation to provide the consumer with personalised pre-contractual information in the form of European Standardised Information Sheet (ESIS) (Article 14 MCD) the model for which is given in Annex II of the Directive. With full standardisation of personalised pre-contractual information, consumers are offered a comparison between the existing credit possibilities available on the market and are thus able to make an assessment of their implications in order to make an informed decision about whether to conclude a credit agreement. Special standardisation of personalised pre-contractual information at the level of the EU is emphasised in the rules binding Member States to transpose the rules on the ESIS (Article 14(2), Annex II) into their national legislation without any variations (maximum harmonisation, Article 2(2) MCD). The obligation of maximum harmonisation refers only to the rules on the use of a standard form.

Other rules on personalised pre-contractual information are subject to either minimum or optional harmonisation. For example, rules on the time period during which the consumer will have sufficient time to make an informed decision are subject to minimal harmonisation. The Directive prescribes that such a period will last at least seven days (Article 14(6) MCD). This means that Member States may determine a longer period for making an informed decision. They thus have an option to decide whether this period of time will be a period of reflection before the conclusion of the agreement, a period for exercising the right of withdrawal, or a combination of the two (Article 16(6) MCD). It actually depends on Member States whether or not a consumer who concludes a credit agreement will be entitled to the right of withdrawal.[61] In such a way, the Directive has made an exception compared to previous consumer directives where consumers were given the right of withdrawal as a separate right after the conclusion of a consumer agreement.

The regulation of the time available as a period of reflection prior to the conclusion of an agreement protects the consumer in a different way because he is granted such a period of time for making an informed decision before entering into an agreement. This is why there is a special option in the Directive if a Member State decides to regulate such time as a period of reflection. To increase consumer protection, a Member State may then provide that consumers may not accept an offer for a period not exceeding

[60] See Ch König (n 7 above) 6.
[61] See Ch König (n 7 above) 5.

the first 10 days of the reflection period (Article 14(6) MCD). In such a way, the protection existing in other consumer contracts where consumers may exercise their right to withdrawal is moved into the pre-contractual phase. Protection is offered in such a way that the conclusion of an agreement is actually prevented until all the relevant information in the form of a standard information sheet has been obtained.

All the rules laid down in the MCD regarding information and practices prior to the conclusion of a credit agreement undoubtedly make it possible for the consumer to make an informed decision on whether to enter into a credit agreement, with whom, and what kind of credit agreement this is going to be. Pre-contractual information to make an informed decision on entering into an agreement is one of the key pillars of consumer protection in the EU. In this particular sector, consumer protection is constantly increasing. Specific obligations regarding information are introduced in the phase of advertising and offering general information. Maximum harmonisation is envisaged for the rules on the pre-contractual provision of necessary information. Special forms for such information are being standardised and the lists of those that are compulsory are extended. The MCD follows all the trends already existing in the previous consumer contracts directives[62] and in particular those contained in the Directive on Consumer Rights of 2011,[63] where the obligation of pre-contractual information was raised to the level of a general rule for all consumer contracts (Article 5), while for distance and off-premises contracts there is a special list of pre-contractual information requirements as a maximum harmonisation rule (Article 6).[64] Compared with the rules on pre-contractual information for distance and off-premises contracts laid down in the Directive on Consumer Rights (Article 6), the MCD provides for the content of pre-contractual information in an even more complex manner.[65] In the very text of the MCD, not all information that must be given to a consumer is listed (as in the Directive on Consumer Rights, Article 6(1)), but the obligatory list of pre-contractual personalised information is derived from the European Standardised Information Sheet (ESIS). All these pieces of information are

[62] See eg Consumer Credit Directive (n 48 above), or Directive 2008/122/EC of the European Parliament and of the Council of 14 January 2009 on the protection of consumers in respect of certain aspects of timeshare, long-term holiday product, resale and exchange contracts [2009] OJ L33/10.

[63] Directive 2011/83/EU of the European Parliament and of the Council of 25 October 2011 on consumer rights, amending Council Directive 93/13/EEC and Directive 1999/44/EC of the European Parliament and of the Council and repealing Council Directive 85/577/EEC and Directive 97/7/EC of the European Parliament and of the Council [2011] OJ L304/64.

[64] The obligation of pre-contractual information does not apply to consumer contracts exempted from the area of application of the Directive on Consumer Rights (Art 3(2)) or for distance and off-premises contracts in the case of which pre-contractual requirements are particularly provided for in this Directive (Art 6).

[65] Comp Annex II MCD.

adjusted to the particular data of the parties and their obligations arising from the loan credit agreements (amount and currency of the loan, the borrower's rights, interest rate, other costs, the number of payments, etc) and they must offer a complete picture of the borrower's rights and obligations, and all financial and legal consequences for the borrower in the case of the non-fulfilment of obligations. A standardised form in which information is provided contributes to better understanding. However, despite such a clear presentation of information in the ESIS, it is questionable whether one can expect the average consumer to be able to read and understand all the information contained on the information sheet and to make an informed decision whether to enter into a credit loan agreement. The complexity and amount of data may ultimately discourage consumers from entering into such agreements, and, what is even worse, this may result in contracts being concluded without the necessary understanding of the conditions of taking loans. Therefore, a particularly important provision is the one contained in Article 16 MCD on adequate explanations. The MCD lays down that Member States must ensure that the creditor, credit intermediaries and appointed representatives must provide adequate explanations to the consumer, such as those about the essential characteristics and specific effects of the credit, including the consequences of default in payment (Article 16 MCD). Such additional explanations, if the consumer asks for them, may lead to informed decisions being made on the loan which satisfies the consumer's needs and his or her financial situation.

iv. Standardised Calculation of Annual Percentage Rate of Charge (APRC)

A particularly important measure for the prevention of irresponsible borrowing is full and timely information for consumers of the total cost of credit throughout its duration. Very important is the information on the annual percentage rate of charge (APRC) and the method of its calculation. Therefore, the Mortgage Credit Directive, like the Consumer Credit Directive, prescribes a standardised calculation of the annual percentage rate of charge (Article 17).[66] In order for the consumer to be fully informed about the method of calculation and the total amount of his debt ahead of time, the Directive lays down a mathematical formula (Annex I) for the calculation of the APRC. It is expressly prescribed that the calculation must be based on the assumption that the credit agreement is to remain valid for the period agreed (Article 17(3)) and what costs must be included in the total cost of credit (Article 17(2)). The rules set forth in the Directive on the method of calculation of the annual percentage rate of charge

[66] See Ch König (n 7 above) 7.

(Article 17(1)–(5), (7), (8)) are the rules subject to maximum harmonisation (Article 2(2) MCD). Member States are not allowed to provide a different method of calculation of the interest rate and the total cost of credit in their national regulations and they may not allow consumers to waive the rights conferred on them ensuing from the rules on the calculation of the interest rate (Article 41 MCD). After the Directive has been transposed into national law, creditors will be bound to calculate interest rates only by using the formula and the method prescribed in the Directive. In such a way, legal security, certainty, transparency and product comparability will be established in credit agreements relating to residential immovable property.[67] The possibility of using different methods of calculation of interest rates and altering them for the duration of the credit agreement will be excluded.

v. Obligation to Assess the Creditworthiness of the Consumer

The creditor's obligation to verify the creditworthiness of the consumer before concluding a credit agreement is specifically regulated in the MCD as a measure by which irresponsible lending is prevented. When transposing the Directive in their national legislation, Member States must establish separate rules by which they bind creditors to make a thorough assessment of the consumer's creditworthiness (Articles 18–21 MCD). This is an essential condition on the part of creditors to be able to make informed decisions whether to enter into a credit agreement with a particular consumer. The basic criterion for such a decision will be an impartial, objective, independent and documented valuation of all factors important to verify the prospect of the consumer meeting his obligations under the credit agreement (Article 18(1) MCD). The Directive expressly provides that such assessment of creditworthiness will not rely predominantly on the fact that the value of the charged immovable property is higher than the amount of the credit (Article 18(3)) but that other reliable standards have also been taken into account for the valuation of the immovable property, such as the consumer's income, expenses and other financial and economic circumstances. However, particular importance in the Directive is given to the valuation of residential immovable property that will be encumbered by mortgage (Article 19). Creditors must use reliable standards for property valuation, and the appraisers who carry it out must be professionally competent and independent of the credit underwriting process.

The basic condition for a detailed and objective assessment of the creditworthiness of the consumer is the possession of all information relevant for the assessment. The sources of information specified in the Directive come

[67] See HJ Dübel and M Rothemund (n 34 above) 3.

from all relevant internal and external sources, including the information provided to the creditor by the consumer, an intermediary, or appointed representative. They include access to databases used in all Member States for the assessment of creditworthiness (Articles 20, 21 MCD). Therefore, Member States must expressly provide for the consumer's obligation to submit, in the pre-contractual phase, all the information and evidence that creditors specify as essential for the appropriate assessment of creditworthiness. Regarding access to databases, Member States must provide access to the databases used for the assessment of creditworthiness to all creditors from all Member States, regardless of whether they are operated by public or private registers.

The assessment results determine the creditor's actions with regard to the credit application. If the creditor finds that the consumer will not be able to fulfil his obligations under the credit agreement, he must reject the credit application.[68] When transposing the Directive, Member States must establish separate rules providing for such a creditor's obligation. The mere fact that the consumer has given insufficient data to the creditor may not be the basis for the termination of the credit agreement, but Member States may prescribe that termination is allowed if the consumer knowingly withholds or falsifies information (Article 20(3) MCD).

The assessment of the creditworthiness of the consumer is by all means one of the very important conditions for an informed decision on whether the creditor will accept or refuse a credit application. The MCD very broadly determines the sources which help the creditor to acquire all the relevant information on the creditworthiness of the consumer (Article 20). These are not only the information given to the creditor by the consumer him or herself, but also the information from different public and private databases used in individual Member States to assess the creditworthiness of consumers and to monitor the observance by consumers of credit obligations. However, we must not forget that these are the consumer's personal data that need to be protected. The MCD does not contain any special provisions on the liability of the creditor for the use of the consumer's personal data from a database. The only thing that is provided for in the MCD is that the provisions on the access and disclosure of a database and the verification of consumer information are without prejudice to Directive 95/46/EC on the protection of individuals with regard to the processing of personal data and on the free movement of such data (Articles 20(5), 21(3) MCD). In other words, the protection of the consumer's personal data should be provided by the measures of the Member States for the implementation of Directive 95/47/EC. Taking into consideration the specific characteristics of

[68] The creditor would not be in a position to subsequently cancel or alter the credit agreement because of irregular assessment, unless the consumer consciously withholds or falsifies information (Art 18(4) MCD).

the data kept in various credit registers, more efficient consumer protection would require the special organisation of personal data protection in the process of assessing the creditworthiness of consumers This is of particular importance because, according to the MCD, consumers' data on their creditworthiness may also be used in cross-border credit agreements.

B. Measures for the Prevention of Defaults and Foreclosures

The protection of the consumer for the duration of the credit agreement is primarily directed at ensuring the conditions necessary for the regular, timely and complete fulfilment of credit obligations, particularly in situations where, after the conclusion of the credit agreement, particular circumstances occur which have a negative impact on the possibility to fulfil credit obligations. In principle, these are alternative measures by which consumers are assisted when they have difficulty in fulfilling their credit obligations. On the one hand, some of these alternative measures are regulated in individual Member States with the help of dispositive norms of the law of obligations, and the parties may incorporate them in their credit agreement. On the other, the incorporation of these measures in the credit agreement is expressly prohibited in other Member States of the EU. Indeed, the aim is to provide for greater protection of the consumer/debtor, although in the end, this makes his or her position even more difficult if he or she is unable to fulfil the obligations arising from the loan.[69] The current Directive lays down common standards for some of these alternative measures, and if these standards are observed, consumers are allowed to make use of these measures. In the Directive, particularly important measures for the prevention of defaults and foreclosures are specific consumer rights in the case of foreign currency loans, such as the right to early repayment, the right to agree on the transfer of the charged residential immovable property, or the right to the proceeds from the sale to repay the credit, as well as the measures for forbearance before and during the foreclosure proceedings.

i. Foreign Currency Loans

Entering into credit agreements relating to residential immovable property in foreign currency loans is a very common practice in some Member States. The biggest problem with such loans is the protection of consumers against the exchange rate risk which significantly increases credit obligations and

[69] See below under III.B.iii on contracting the right to agree the transfer of charged property to repay the credit.

ultimately leads to the consumer's insolvency.[70] Because of such changed circumstances, protection of consumers is possible by the application of the general rules of the law of obligations. It is also possible to agree that some protection clauses be entered in the loan agreement in accordance with the national law. In practice, such national measures do not provide sufficient consumer protection, partly because of specific conditions for their realisation, and partly because of the insufficient level of information on the part of consumers. In order to harmonise the rules on the protection of consumers against exchange rate risks, the Directive binds Member States to expressly provide for the regulatory framework of consumer protection when concluding foreign currency loans (Article 23).

This commitment to protect consumers against exchange rate risks is resolved in the Directive in a very specific way. The basic right that consumers must have when taking foreign currency loans is the right to convert the credit agreement into an alternative currency,[71] or the right to make other arrangements to limit the exchange rate risk (Article 23(1) MCD).[72] The concrete regulation of consumer protection within the framework established in the Directive is left to individual Member States. They may recognise both options or only one of them. They may also regulate these rights in such a way that they allow *creditors* to specify whether the consumer is left with both choices, or with only one of them (Article 23(2) MCD). In the case of the option of 'other arrangements to limit the exchange rate risk', Member States are completely free to choose and regulate such arrangements. The Directive only prescribes that the purpose of such arrangements must be to limit the exchange rate risk, and the rules on the imperative nature of the Directive (Article 41) provide that the consumer may not waive these rights.

Consumers' rights aimed at limiting exchange rate risks are extremely important for the prevention of consumer over-indebtedness, arrears and foreclosures. Various problems arising in practice due to changes in exchange rates have resulted in situations where in some Member States

[70] The Commission's proposal for a Directive on credit agreements relating to residential property of 2011 did not provide for the protection of consumers when taking foreign currency loans. Special rules on consumer protection have been incorporated in the Directive as an amendment by the European Parliament.

[71] An alternative currency is either the currency in which the consumer primarily receives income or holds assets from which the credit is to be repaid, or the currency of the Member State in which the consumer was either resident at the time the credit agreement was concluded, or in which he is currently resident (Art 23(2) MCD). In the case of the conversion of a credit agreement into an alternative currency, the exchange rate at which the conversion is carried out is the market exchange rate applicable on the day of the application for conversion, unless otherwise specified in the credit agreement (Art 23(3) MCD).

[72] The basic condition for the realisation of the right by which the consumer is protected against an exchange rate risk is his being well informed about the risk. In line with this requirement, the Directive puts an obligation on Member States to bind creditors to warn consumers of the changes of the exchange rate at least where the value of the total amount payable by the consumer varies by more than 20% (Art 23(4) MCD).

special measures have been taken to prevent over-indebtedness.[73] The efficiency of the measures referred to in Article 23 MCD primarily depends on how they are implemented at the national level in different Member States. Article 23 leaves Member States with very broad possibilities regarding consumer protection, as well as different options. Some of them have not even been sufficiently defined in the MCD. For example, the MCD does not define in any way and does not give any examples of which 'other arrangements' would be appropriate for consumer protection, apart from the conversion of loans into an alternative currency. Moreover, the MCD leaves it to Member States to allow creditors to determine the possibilities available to consumers to protect themselves from currency rate changes (Article 23(1)). Finally, Member States are given the possibility to additionally regulate foreign currency loans under the condition that these regulations do not apply retroactively (Article 23(3) MCD). This can certainly not solve the problem of the already existing over-indebtedness of consumers on the basis of existing housing loans resulting from current foreign exchange differences. Such an approach in the regulation of a very important consumer right when it comes to foreign currency contracts appears insufficiently concrete to ensure, at the national level, appropriate consumer protection from changes in foreign currency rates. The final result of consumer protection at the national level will thus largely depend on how individual Member States balance the protection of consumers' interests on the one hand, and that of creditors on the other. In a very specific way, the MCD opens up possibilities for giving a certain kind of precedence to creditors' interests if the possibility of deciding whether these possibilities referred to in the MCD, or only some of them, are available to consumers.

ii. The Right to Early Repayment

A special measure of consumer protection in the execution of credit agreements laid down in the Directive is the recognition of the consumer's right to early repayment of the loan with a reduction consisting of the interest and the costs for the remaining duration of the contract (Article 25). In their national legislation, Member States must regulate the right to early repayment, ie the right to discharge fully or partially their credit obligations prior to the expiry of the credit agreement (Article 25(1) MCD) as a special consumer right in credit agreements relating to residential immovable

[73] Eg, in December 2013, the Republic of Croatia, shortly after having become a full Member State of the EU (1 July 2013), amended the Consumer Credit Act (2009), by which the Consumer Credit Directive was implemented with the provision on the protection of consumers from changes in exchange rates. The Croatian Consumer Foreign Currency Housing Loans Act lays down a maximum amount of variable rate credit if the exchange rate changes by 20% or more. There is also a provision binding creditors to offer the conversion of loans into the domestic currency (Art 11(a)).

property.[74] The exercise of this right must not be subject to any sanctions. However, the regulation of all other conditions and modalities for the realisation of the right to early repayment continues to be left to Member States. For example, Member States may provide that the creditor is entitled to fair and objective compensation, which must not exceed the financial loss caused by early repayment of the loan. Member States may also provide restrictions, special conditions and time limitations under which the right may be exercised, as well as different treatment depending on the type of the borrowing rate or on the moment the consumer exercises the right to early repayment, and the like.

As with consumer protection involving foreign currency loans, the regulation of the right to early repayment at the national level leads to large differences which may have a strong impact on the level of consumer protection. The legal regulation of early repayment depends on how every individual Member State assesses the optimum level of the protection offered to consumers, or whether the right to early repayment has certain conditions and limitations, and whether the creditor, in such situations, is entitled to direct and objective compensation (Article 25(3) MCD). Indeed, the MCD provides that the compensation to be given to the creditor should not exceed the creditor's financial loss. However, the question still remains about whether, by prescribing such additional conditions for exercising the right to early repayment, consumers are discouraged from exercising their rights. In order to achieve better consumer protection, it would be much better for the MCD to contain a legal framework within which the right to early repayment may be exercised. It now seems that the right to early repayment is only declared as one of the consumer rights in credit agreements, but the circumstances still do not exist for the harmonisation of that right at the EU level.

iii. The Right to Agree on the Transfer of Charged Residential Immovable Property to Repay the Credit

One of the oldest traditional measures of consumer protection is the prohibition imposed on the parties to contract in advance that the charged real property will be transferred to the creditor's ownership if the debtor does not pay the debt in due time, and that in such a way the secured claim will be settled (the so-called *lex commissoria*). Such a clause is prohibited to protect the debtor as the weaker party to a mortgage agreement, and to prevent creditors from insisting that such a clause be entered in the mortgage agreement. Therefore, many national laws prohibit the incorporation

[74] The so-called 'pre-payment option' is considered as a measure ensuring financial and physical mobility of European consumers. See HJ Dübel and M Rothemund (n 34 above) 4, 60.

of such clauses before the repayment is due. Upon maturity, the possible transfer of ownership of the charged immovable to the creditor instead of the repayment of the loan is governed by the rules on the so-called *datio in solutum*.[75] Because of the financial crisis and the inability to make regular and timely payments arising from credit agreements relating to residential immovable property, the approach to the problem of the repayment of loans by transferring ownership of the charged immovable has become more liberal. In some cases, particularly when residential immovable property is at issue, it is believed that regulation of the right to free a debtor of his credit obligations by way of transferring the ownership of the charged immovable to the creditor may be more beneficial for the consumer than if enforcement proceedings for the repayment of the loan are conducted against him.[76]

Such a liberal approach to the possibility of contracting the transfer of ownership of an immovable as a substitute for the repayment of the credit is also laid down in the MCD. The Directive binds Member States not to prevent an express agreement that transferring the charged immovable to the creditor, or the proceeds from the sale, are sufficient to repay the credit (Article 28(4) MCD). In other words, the consumer and the creditor may expressly contract that by transferring the ownership of the residential immovable property to the creditor, all obligations from a credit agreement are deemed to have been met. The Directive does not say that the Member States must make it possible for the consumer to make a unilateral statement to free himself of his credit obligations by transferring the ownership of a charged immovable to the creditor, but only that they must allow for the possibility to contract a clause on the transfer of ownership based on the mutual consent of both the consumer and the creditor. It is not clear from the provisions of the Directive whether such an express agreement is allowed only after the credit obligations have matured, ie in the phase of foreclosure, or whether it would be possible to make such an agreement in advance, before the maturity of the credit obligations. The obligation of Member States to allow such an express agreement on the transfer of the charged residential immovable property to repay the credit is provided in the Directive on Arrears and Foreclosures, which leads to the conclusion that at least at the stage of enforcement it should be possible to expressly contract the transfer of the ownership of a charged immovable instead of repaying the credit. However, because Article 28 of the Directive is a provision

[75] For more, see in the 'Study on the 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 Economics (2012) 106–54, 201–18: http://ec.europa.eu/internal_market/finservices-retail/docs/fsug/papers/debt_solutions_report_en.pdf.

[76] See the 'Study on the Means to Protect Consumers in Financial Difficulty' (n 75 above) 204–13, 218.

of minimum harmonisation, it seems that Member States may broaden such consumer protection to include the time prior to the maturity of the credit obligations.

iv. Measures Before the Foreclosure Procedure

The Directive binds Member States to take particular measures to prevent the foreclosure procedure for the payment of claims arising from credit agreements, ie by which the position of consumers in foreclosure proceedings will be alleviated as much as possible (Article 28 MCD). The Directive obliges Member States to adopt measures to encourage creditors to exercise reasonable forbearance before the foreclosure proceedings. The selection of appropriate measures to ensure considerate creditor action is left to the discretion of individual Member States. Every Member State must lay down whether a creditor is entitled to charges because of the consumer's default. In that case, only the charges necessary to compensate for the creditor's costs may be sought. Regarding the foreclosure proceedings to sell residential immovable property, the Directive obliges Member States to adopt measures by which the best price for the charged immovable can be achieved in the foreclosure proceedings. When the creditor still has not been fully compensated in the foreclosure proceedings, Member States must adopt special measures to make it easier for the consumer to pay the remaining debts also after the sale. However, the Directive does not expressly lay down what measures should be introduced at the national level in order to achieve all these goals in the foreclosure proceedings. Therefore, the measures and their content, as well as their realisation, primarily depend on how the foreclosure proceedings are regulated in a Member State and by which instruments within the foreclosure proceedings debtors are normally protected. If the existing measures do not provide efficient protection of consumers in the foreclosure proceedings,[77] in order to act in conformity with the obligations

[77] A very important aspect of the protection of a consumer whose residential immovable property is sold in foreclosure proceedings for the repayment of debts arising from a credit agreement is the legal instrument (eg legal action, complaint, appeal, or an interim measure) by which the consumer in foreclosure proceedings may exercise the protection of his rights, challenge the validity of a credit agreement, unfair contract terms, etc. All these instruments must be regulated in such a way that they offer the consumer efficient protection of his rights. See eg Case C-415/11 *Mohamed Aziz v Caixa d Estalvis de Catalunya, Tarragona i Manresa* (*Catalunyacaixa*) [2013] ECR nyr. This case concerns the interpretation of the principle of the efficiency of interim relief in mortgage enforcement proceedings for the payment of a claim arising from a consumer mortgage credit agreement. For more on the meaning of the principle of efficient consumer protection when dealing with unfair contract terms, see in N Reich, *General Principles of EU Civil Law* (Cambridge, Intersentia, 2014) 89–129; J König, *Der Äquivalenz- und Effektivitätgtundsatz in der Rechtsprechung des Europäischen Gerichtshofs* (Nomos, 2011) 205–11; P Rott, 'The Court of Justice's Principle of Effectiveness and its Unforeseeable Impact on Private Law Relationships' in *The Involvement of EU Law in Private Law Relationships*, ed D Leczykiewicz and S Weatherill (Oxford, Hart Publishing, 2013) 181–98.

in the Directive, it will be necessary to introduce some new measures for consumer protection. The Directive does not specify these measures and it does not even lay down the criteria to be followed by Member States when assessing the existing measures and introducing new ones to alleviate the position of consumers as debtors.

IV. CONCLUSION

Once the Mortgage Credit Directive is transposed into the national legislation of Member States, it will undoubtedly contribute to the greater protection of consumers when they conclude credit agreements relating to residential immovable property, both in the pre-contractual phase and in the phase of fulfilling their credit obligations.[78] This Directive declares high standards in terms of consumers being well-informed and thus being able to make informed decisions when entering into credit agreements. In the phase of the fulfilment of their credit obligations, consumers are offered a number of different measures to facilitate the fulfilment of such obligations and to minimise potential credit risks. It is to be expected that the realisation of these measures will have a positive impact on consumer trust in the housing loans market. In that sense, the Mortgage Credit Directive is by all means a step forward in the process of establishing a single market for residential mortgage credits.

However, it was been argued here that the implementation of the Directive will open many new questions regarding consumer protection when taking home loans. First of all, a question remains about whether the implementation of the Directive will really contribute to an increase in cross-border home loans. It is also uncertain to what extent the implementation of the Directive will really contribute to a more transparent, legally secure and competitive single market of loans relating to residential immovable property. It seems that even after the implementation of the Directive, a great diversity of national rules on mortgages and residential mortgage credit agreements will continue to exist, which may discourage consumers from the cross-border conclusion of credit agreements. The Directive harmonises only some aspects of credit agreements relating to residential immovable property. Minimal harmonisation is what is mostly foreseen. Even where minimum harmonisation is envisaged, the Directive leaves it to Member States to choose from various options offered as a compromise, or specific possibilities for the regulation of individual rights of the parties to credit agreements. In some cases, it is left to Member States to allow creditors to choose which proposed options they want to offer to consumers. Therefore, it seems that even after the transposition of the Directive, significant differences in the national regulation of credit agreements relating to

[78] See Ch König (n 7 above) 13.

residential immovable property will remain. This will be reflected in different levels of consumer protection in the national markets of Member States.

It is also uncertain whether the implementation of the Directive will provide the level of consumer protection needed when consumers take home loans because of the high level of over-indebtedness of consumers resulting from the economic crisis. A question also arises as to whether the implementation of the Directive can contribute to solving the problems that consumers who have already taken home loans face and against whom foreclosure proceedings have already started. Although the Directive contains a series of measures aimed at better consumer protection when consumers take home loans, most of them are set forth in a very general way. This may lead to problems when they are made concrete and when they are implemented at the national level. In the end, it may make the accomplishment of the main goals of the Directive more difficult. Efficient consumer protection when consumers enter into credit agreements relating to residential immovable property at the EU level requires a different approach to harmonisation—an approach where individual consumer rights and the conditions for their realisation are regulated in a more concrete way, and the scope of maximum harmonisation is also extended to other aspects of the contract rather than being limited only to pre-contractual information and the calculation of the APRC. Because of the present need to protect consumers from over-indebtedness, it is not enough to determine generally consumer rights and other measures to be taken to protect them. Likewise, it is not sufficient to bind Member States to adopt measures encouraging creditors to act with reasonable forbearance towards consumers, or measures to facilitate repayment in order to protect consumers. Better protection of consumers as the weaker contractual party could certainly be achieved by concrete and clear rules governing their rights when entering into credit agreements, and possibly also by the extension of consumer protection at least to some aspects of contracts establishing security rights regarding credit claims. In the MCD, only some consumer rights in credit agreements are regulated. This Directive does not provide for any aspect of consumer protection in agreements establishing mortgage or other security rights, although most frequently, in the cases of non-payment, forceful collection is carried out against the mortgaged immovable. The consequences of irresponsible borrowing and lending can best be seen in proceedings for the forced sale of mortgaged immovables, because very often these proceedings end with the repossession of the residential immovable in favour of creditors or third persons. Therefore, the MCD can only be considered as the first serious step in taking the necessary measures for efficient consumer protection on mortgage credit markets. More efficient and complete protection will only be achieved when individual consumer rights arising from credit agreements and mortgage agreements are more thoroughly provided for and when a higher level of harmonisation of the rules is achieved at the level of the entire European Union.