



# FACING UP TO THE FINANCIAL CRISIS

BEUC's concrete suggestions  
to protect consumers in the short and long term

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## Summary

This document sets out BEUC's position on the financial crisis which started in the US and then spread worldwide. The main reason for this contamination lies in under-regulated and under-supervised financial systems, which put immediate financial rewards before companies' stability and risk evaluation.

Consumers are the least protected group in the financial crisis; their rights are violated and their interests often not taken into account. Consumers have lost confidence in deposit, credit and investment service providers, which weakens the basis of the single market and prevents them from cross-border shopping for financial services.

In order to protect consumers and restore their confidence, BEUC proposes a package of measures dealing with regulation and supervision of financial institutions, pre-contractual information and financial advice, responsible lending, deposit guarantee schemes, corporate governance, legislation on financial intermediaries and collective redress.

## INTRODUCTION

The current global financial crisis is causing widespread concern in around the world. Across the EU serious concerns now exist over the future of consumers' personal savings, loans and pension plans.

Many BEUC members have taken measures to address the huge amount of consumers' questions and concerns, such as:

- VZBV (Germany): Specific phone hotline October to December 2008 for 8 weeks (about 140 000 calls).
- Test-Achats (Belgium): in October 2008 the number of phone calls was threefold of that during normal time; the number of fax, mails and letters was fourfold; a petition signed by 7000 persons related to the Kauping bank case was presented to Luxembourg's Prime Minister.
- Altroconsumo (Italy): information related to the financial crisis has been posted on the association's website.
- Consumentenbond (the Netherlands): contact with consumers increased; , they received significantly more questions about financial products such as saving accounts, life insurances, mortgages and pension schemes; a dossier on the financial crisis with Q&A's, news and relevant test-information was placed on the association's website.

BEUC views the current crisis as the failure of an excessively deregulated free financial services market in the US that should not have been duplicated in the EU. When safeguards are removed, the priority given to the pursuit of corporate profit and personal gain leads to widespread irresponsible risk-taking that is now impacting on the whole economy.

There is also a need to question the role of financial service providers. Some of them have forgotten to fulfil their pivotal base functions and to maintain stronger and adequate safeguards for these functions: one could think of dividing banks into "down-to-earth banks" that provide these base functions and "investment banks" that take on higher risks...

European Institutions must now take urgent action to protect consumers' deposits and investments and ensure that credit continues to be available on fair terms. Consumers with savings need to be confident that their money is safe during this unprecedented crisis. Consumers who have taken out loans for homes must not have the loan foreclosed due to failings in the system which has not been able to assume its responsibilities.

However, the European Institutions' responsibility regarding consumers must go further taking into account banks and institutions that are at the edge of bankruptcy. They must also take action to restore responsibility, accountability and transparency to national and European financial markets.

Regulation should place consumer protection above market pressure for short-term profit maximisation.

BEUC is concerned by the prices consumers are already paying for the errors made by financial institutions and supervisors who failed to fulfil their responsibilities: access to credit has become more and more difficult to consumers; cuts on interest rate have not been passed-on onto consumer credits; bank account fees are increasing, etc.

In order to restore consumers' confidence in the financial sector, the consumer interest should be taken into account within all initiatives that are currently being discussed to solve the current crisis and to avoid a new one.

## **FINANCIAL SUPERVISION AND REGULATION**

### ***Facts:***

The current financial crisis has shown that national supervising authorities have not been capable of correctly detecting the risks and imposing the necessary measures to avoid this crisis. Host state<sup>1</sup> supervisors have little to no influence over the regulation of passporting firms<sup>2</sup>. If some national supervisors are not doing their job properly consumers are put at risk. Cooperation between national supervisors regarding largest banking groups is supposedly already taking place, but smaller banks like Landsbanki and Kaupthing bank seem to have slipped passed the radar. A number of outrageous financial swindles have been witnessed recently (for example the Madoff scandal) which have obviously not been detected on time.

BEUC does not call for more legislation and regulation as such, but for more adequate, effective and efficient legislation and financial regulation.

New products need to be evaluated for risks to see how suitable they are for consumers and the market. It may be necessary to label products belonging to certain risk categories, to make consumers think twice.

### ***Our demands:***

- More powerful and independent national supervisors are needed everywhere in the EU.
- In order to provide better protection to consumers, national supervisory bodies should fulfil the following functions: participate in advertising control, control of financial information, unfair practices (bundled and tied products), distribution of financial products (for example in the area of consumer credit); take charge of an early warning system (inform consumers about the risks/risk category of various financial products on the basis of continuous enquiries).
- Since the development of financial services has led to the emergence of universal actors providing a wide range of financial services (for instance, together with their traditional role, banks offer more and more insurance services, investment products, etc.) it is not necessary to have a large

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<sup>1</sup> Country in which a foreign service provider is doing business.

<sup>2</sup> Firms having an EU passport are allowed to work freely throughout Europe regardless of their place of establishment.

number of supervisory authorities. A unique supervisor is needed to cover all financial services and all financial institutions (banking and non-banking). Therefore, there is a need to merge existing national supervisory authorities (bank/non bank credit, insurances, securities/pensions funds).

- Strengthen the cooperation between national supervisors and regulators: create a binding network between them (see for instance the Regulation on consumer protection cooperation).
- As financial systems and markets are becoming more and more integrated, it is necessary to create a financial supervision authority in charge of control of financial institutions operating at cross-border level, whatever their size is (for example Icelandic banks).
- Adopt binding rules at EU level so that all Member States are obliged to comply with them. Soft law has shown its limits especially in case of financial services. Therefore, the regulatory gaps must be filled in.

## **PRE-CONTRACTUAL INFORMATION ON FINANCIAL PRODUCTS AND SERVICES**

### ***Facts:***

The crisis has shown that the information offered to consumers is not adequate. Consumers have access to information which is often very long and not consumer-friendly (consumer-oriented); it does not help them to compare products and to make the right choice.

### ***Our demands:***

- Provide information to the consumer well in time before the contractual decision.
- Make information shorter (no more than 2 pages) but understandable, structured, and with comparable relevant information on all the essential key features. Information obligations should be reviewed closely to achieve this goal (the current CESR work on the UCITS Key Investor Information and the Focus Groups could be a model).
- Create a single risk indicator for investment products. For instance, in France the "Caisse d'Épargne" has introduced traffic light labelling, informing investors on risk level (and sustainable consumption aspects). The experience of risk labelling of financial products exists also in the Netherlands. Such indicator should include the following information:
  - a) Whether or not the invested capital is guaranteed.
  - b) Investment volatility.
  - c) Information on suggested retention period for the expected return to compensate for the volatility risk.
- Introduce stricter rules on marketing and advertising practices especially for investment products.
- Develop the concept of simplifying and standardising financial services, with features that can be easily recognised and compared.

- At the same time, prevent the service provider from exploiting the information provision to escape their responsibilities: providing complete, understandable and comparable information should not exempt the service provider from their other responsibilities (responsible lending, responsible advice, etc.).

## **FINANCIAL ADVICE**

### ***Facts:***

Financial products are more and more complex. The current crisis has unveiled the problems consumers have to face: even the enlightened consumers have not been able to understand the financial products offered to them (see Madoff's clients). Moreover, everywhere in the EU there is a lack of independent advice that consumer can rely on.

Advice is in general only given by financial service providers and is often not targeted to consumers' needs and expectations but is rather linked to the bank's commercial practices. This creates a conflict of interests which is to the detriment of consumers.

### ***Our demands:***

- Independent advice is necessary to prevent wrong decisions, especially in case of major financial decisions.
  - Funding for independent advisors: should be partly by public authorities (to avoid market failures) and partly by consumers; in any case, advice should be at affordable rates.
  - Advice could be provided by consumer organisations or other independent bodies.
- Responsibility of advisors (service providers and independent advisors):
  - Set up a MiFID<sup>3</sup> profile for each investor. If the product does not match the profile, a warning to consumers should be emitted.
  - Ensure information given to consumers is reliable.
  - Effective documentation of the advice should be given to the investor.
  - Make it easier for consumers to claim compensation (the burden of proof should lie with the advisor).

## **CREDIT – RESPONSIBLE LENDING**

### ***Facts:***

Irresponsible lending is one of the main causes of the current financial crisis. As a consequence, more attention should be paid to this issue. Lenders should be

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<sup>3</sup> The Markets in Financial Instruments Directive.

obliged to assess the financial capacity of consumers asking for a credit and check their creditworthiness.

***Our demands:***

- Regulate variable interest rates to protect consumer from interest burden:
  - Cap variable interest rates to limit interest rate variations.
  - Improve information on variable rates.
  - Prohibit promotional rates, i. e. attractive (or fixed) interest rates that switch to higher (or variable) interest rates after a certain period of time.
- Foster consumer protection and responsible behaviour of credit institutions with legislation on mortgage credit: if the bank's decision is based on a poor quality assessment of consumer's financial situation the costs of irresponsible lending should be bared only by lenders and not by consumers (see Belgian law on responsible lending).
- Regulate crediting activities that seriously endanger the solvency of consumers (foreign currency credit, credit secured with mutual funds, Lombard credit, revolving credit...) as well as usury rates and excessive costs.
- Accompany and evaluate closely the implementation of the Consumer Credit Directive with a specific focus on the level of consumer protection (including the regulation of credit distributors), a responsible credit business and necessary adjustments in the future and monitor specifically the transposition and implementation of Article 8 (lender's obligation to assess the creditworthiness of the consumer).

## **DEPOSIT GUARANTEE SCHEMES**

***Facts:***

At the moment, deposit guarantee schemes work extremely inadequately at cross-border level. What happens when banks have the European passport in their home country but do 99% of their business cross-border? No lessons have been learned from the current crisis: the new rules do not take into account the internal market dimension of the issue at all. This could discourage consumers from cross-border shopping for financial services.

***Our demands:***

- Make deposit guarantee schemes work cross-border:
  - Consumers' deposits should be equally guaranteed across Europe, whatever the service provider's location is.
  - Payout procedure should be as easy as it is at national level, especially in terms of delay.
- Ensure the maximum harmonisation of deposit guarantee schemes with complete coverage of deposits all over the EU, in order to avoid an uneven competition among schemes.

- Review the Directive on Investor Guarantee Schemes in order to protect investors in the same way as depositors.

## **CORPORATE GOVERNANCE**

### ***Facts:***

The financial service providers have to understand that they have a unique responsibility in the economy; they provide the necessary means for money to circulate. On the contrary, over the past years, many banks have started to think that they are there to make money and provide jobs for those who want to join the joy-ride.

The way in which CEOs and especially intermediaries who sell non-efficient and not-suitable products (because they earn substantial commissions by selling these products) of certain financial companies are remunerated encourages them to seek short-term profits without taking into account the long term effects of their decisions on their clients.

### ***Our demands:***

- Strict rules and supervision must be developed at EU level, using best practices, for financial institutions to behave in a responsible way:
  - Particularly abolish variable remuneration schemes based on short term performance and replace them by long term commitment of executives to the companies they work for.
  - Transparency and accountability of managers' remuneration.

## **HARMONIZATION OF LEGISLATION ON FINANCIAL INTERMEDIARIES**

### ***Facts:***

Many financial intermediaries sell complex financial products without having any qualifications, and are not accountable in case of failure of the product.

### ***Our demands:***

- Introduce rules to limit initial commissions.
- Ensure harmonisation of rules for intermediaries, regardless of what they are selling.
- Introduce rules on registration, qualification, transparency, liability and insurance.

## **REDRESS**

### ***Facts:***

In a study carried by the European Commission it has been shown that 39% of consumers find financial services being the sector in which it is most difficult to obtain redress. The current crisis has demonstrated that various practices such as lack of information, marketing of risky products, irresponsible lending, etc. can affect at the same time a very high number of consumers that are not compensated for the damages they incur.

In addition, there are no easy mechanisms everywhere in the EU allowing individual consumers to get their disputes solved.

### ***Our demands:***

- Establish a Group Action procedure allowing a number of consumers to bring a case together to court to obtain compensation for a damage caused by the same provider both at national and cross-border level.
- Put in place simplified mechanisms for individual redress working efficiently both at national and cross-border level.

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